THE

Principles of Bookkeeping

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PREFACE

IT may be thought that some apology is needed for the appearance of another book upon the subject of Bookkeeping. It is true that within the last few years many and able books have appeared which have raised the tone of thought upon, and led to the more scientific treatment of the subject, but this is no reason why we should object to the appearance of further publications; and so long as a great majority of people remain practically ignorant of the more advanced and theoretical parts, it is likely that renewed attempts will continue to be made to advance and expound it as a science. The whole mercantile and governing world are absolutely dependent upon the assistance afforded by Bookkeeping. A thorough knowledge, therefore, of the science is most useful, is not difficult to acquire, and yet, at the same time, is a most surprisingly rare attainment. Important, then, as the study is, people will not object to the number of books about it, if only each may be fortunately found to contain some little additional help towards the elucidation of a good and useful system. It is hoped that the following pages, though, perhaps, containing nothing particularly new, may be found to treat some old truths in a new and condensed manner.

However, the principal apology, if apology there must be, will be the plea urged by the patriarch Lot on behalf of the City of Zoar, and have reference to its smallness. There may still be room for a little one—"Is it not a little one?"

At the same time, much regret is felt for the defects which it is feared may be found in the book.

J. A. C.

Land of Green Ginger, Hull,
5th August 1896.

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The Principles of Bookkeeping.

INTRODUCTION.

AT the outset it is necessary that we should have some clear idea of what we mean by the Principles of Bookkeeping. By Bookkeeping, we mean the recording, analyzing and totalling, of mercantile transactions, with a view to showing a business man the monetary relations in which other people stand to him, his own financial position generally, and to what extent, and through what causes, that financial position has altered from time to time. The Principles of Bookkeeping will, therefore, be the fundamental truths, hypotheses, and rules, which will guide him in recording, analyzing, and totalling, with these important objects in view. For example, as a fundamental truth, we shall see that a transaction has precisely the opposite effect upon one of the parties to it to what it has upon the other party; as a hypothesis, that every credit implies a debit of corresponding amount, and every debit a credit of corresponding amount, whether the first entry taken is the immediate record of a transaction or no; as a general rule, that a column on the left-hand side is used for debit entries, and a column on the right for credit entries.

As it is better to survey your country before beginning to construct a railway than to survey the country from the carriage windows when the line is constructed, so if the bookkeeper makes his mind familiar with the theory or plan of Bookkeeping, he will easily understand what work requires to

be done, and will do that work correctly; but if he is unacquainted with the general purpose and design, he is always liable to occasional error.

Again, as the architect designs his building to fit the shape of his piece of land, so a bookkeeper who understands the principles of his work has not his mind cramped and stunted, and feels at liberty to modify his methods to suit the nature of the business. He has more boldness to judge whether a practice is right or wrong, under the circumstances, instead of simply whether it has been the custom or no.

It would seem, therefore, that the principles should be the first things to be mastered, whereas, in practice, they are frequently the last to be learned. In most offices, although much of the detail of Bookkeeping is performed by the junior clerks, they do not see how the accounts are finally closed; and, though they may be taught to keep the accounts with the customers of the firm perfectly accurate, they do not learn how the impersonal accounts are treated, so as to show the benefits accruing to the firm, for the advantage of which the business is solely conducted. Occasionally, persons are found who have kept books for a long period, but having simply followed on with entries similar to those which had been previously made, they have managed to get through their work without fully knowing the why and the wherefore of it. As we should hardly call a person a musician who could not read music, so we can hardly call a person a bookkeeper who has only learned his work by rote. The consequence is that, if any entries are required of an unusual character, such persons are quite at a loss, and it does not occur to them, or they dare not venture, to make any alteration in their system, even though it may be causing them unnecessary trouble.

As an illustration, the Journal in a business having almost world-wide fame, showed a curious specimen of a minor inaccuracy. The entries were correctly written in and posted,

but the figures had always been put into the reverse columns, making the book rather awkward to work from when in the hands of a stranger. Supposing £100 for rent had become due to John Brown, the entry in this Journal would have appeared :—

		£ s d	£ s d
Rent	*Dr.*	..	100 0 0
To John Brown		100 0 0	

When asked why this was done, the explanation was given that it was so that the posting to the Ledger would come on the reverse side, like the posting from a Cash Book; showing that, to the very last, a misapprehension lingered. Evidently it was not understood that the Cash Book is to be viewed as a Ledger Account, for convenience kept in another book (this will be seen later on), hence the reason for posting on the reverse side; but the Journal, being solely a subsidiary book intended for simply preparing the entries for the Ledger, they should appear in it exactly as they will in the Ledger.

Many a person who has been used to keeping books refrains from the study of a book upon the subject (unwisely, nevertheless) because a book with long examples worked out seems tedious to read, especially as the greater part of the subject dealt with is already familiar to him. But this should not apply to a study of the principles separately.

This book does not profess in itself to teach Bookkeeping, though it would, of course, be contrary to my purpose to detract from the idea of its possible use in that respect, for if the foundation principles are grasped the adaptation of them to ordinary practice is a simple matter. It is hoped, therefore, that the book may be of some little use if it throws a glimmer of light upon the Principles of Bookkeeping.

The first five chapters will be found to deal with the principles underlying the more elementary part of Bookkeeping. The last four deal with topics of a more advanced character,

which are given for the direct use they may be in themselves, and also as serving to give a kind of bird's-eye view of much of the more ordinary part of Bookkeeping. For instance, it will do no one any harm to know how to balance Ledgers separately, even though he may never want to do it; he will be none the less able to balance them as a whole because he knows how to balance them separately. So he will be none the less able to adjust the accounts of a solvent estate because he has some idea how to adjust the accounts of an insolvent estate, just in the same way that, if we would wish to impress our minds with the general shape of a figure, it would be well to look at it upside down as well as right way up.

CHAPTER I.

The Mercantile Transaction and its Double Effect.

Meaning of Transaction—Consideration-Liability attached—Distribution of Wealth depends on Transactions—Wealth the Result of Throwing Consideration-Liabilities in our Favour—Discharging Cross Liabilities—Saleable Goods on hand—Two Accounts affected by a Transaction—Error of neglecting this—A Transaction has Reverse Effect on one Account to what it has on the other.

IT is the province of Bookkeeping to treat of only commercial wealth and indebtedness. Bookkeeping cannot take into account wealth that is not saleable nor moral obligations; it can only deal with values and indebtedness when reduced to terms of money.

The lowest unit of commerce is the transaction; all commercial wealth and indebtedness are the result of individual transactions.

A transaction means the doing of something across, the agreeing to pass something from one person to another. That which passes is one of four things—(1) goods; (2) money; (3) the use of a thing; (4) personal service. As a comet always has a tail attached to it, so the subject of the transaction in passing to the receiver has always a monetary consideration attached (nebulous yet potent) which becomes a liability, or in itself tends to a liability. In the first of the four cases, the consideration-liability is the agreed price of the goods; in the second, the amount of money, with perhaps

a further liability for interest accruing by the year: in the third, the rent or hire accruing from time to time; in the fourth, the wages accruing from time to time. In the third case there is also the responsibility for the return of the thing; but this, of course, is only treated in Bookkeeping when the responsibility changes into a liability through failure to return as agreed. If a transaction does not tend to the creation of a liability by either of the parties, then it must be accounted for in one of two ways: First, that two transactions have taken place simultaneously (each of which, taken separately, would tend to a liability), as when goods are sold and cash paid for them at the same time; or, secondly, the deliverer of the thing has agreed to forego the consideration-liability, and it is not a commercial transaction at all, but a gift. Beggars often profess the liability is still there; this is so when they say, "Lend me 6d." These two cases do not interfere with the above proposition that every commercial transaction tends to the creation of a liability attaching to one of the parties to it. It is the province of Bookkeeping to collect up and give due effect to these liabilities resulting from transactions. This will show us the final amount of indebtedness between traders, and something important besides.

The realisation of commercial wealth depends upon the transactions that are made. The increase of intrinsic wealth (*i.e.*, the possession of useful things) in the world is, we know, due to the operations of nature and the industry of man; but the distribution of it between man and man depends directly upon the transactions made, and the power of nature and industry are only felt in influencing the terms of the transactions. There may be intrinsic wealth in the blade of corn, but it is only when the wheat is ripe and sold that the farmer knows whether he is richer or poorer. So a man may make a good transaction after the bestowal of little industry, and a bad transaction after the bestowal of much industry, and he

is richer or poorer according to the nature of the transaction. If it were not so, there would not be such a tendency to leave off industry and speculate,—that is, make one transaction against another transaction for a chance profit. At the same time, industry should always command a certain amount of power to make favourable transactions. If our labour has improved a thing we may expect a higher price, *i.e.*, a favourable transaction. Thus, as gains or losses are the direct result of transactions, if we duly record transactions we shall also be recording gains or losses.

The process of acquiring commercial wealth consists in arranging that the balance of liabilities resulting from transactions shall be thrown in our favour. Thus, buy a horse for £20; sell it for £25; draw the £25; pay the £20. The profit was fixed when the price (*i.e.*, the liability) was fixed, no matter whether the horse was paid for at the same interview or long afterwards. Indebtedness may be thrown in our favour by one transaction, as, for example, when we agree to work for a week, if the master will become liable to us for £2 at the end of the week; or it may be done by cross transactions, as it would be if we agreed to buy wheat for £1,000, made it into flour, and agreed to sell the flour for £1,100. The consideration-liability resulting from a transaction does not necessarily remain an enforceable liability, because there might be a liability the other way from a previous transaction, or it might be instantly discharged by another transaction (as a cash payment); but it is true that every transaction tends in itself to the creation of a liability by one of the parties to the other, and, therefore, if we keep due record of all these tendencies to liability by one party to the other we shall then know what is the enforceable liability between them. It is also true that profits or losses depend upon whether the balance of these consideration-liabilities is thrown in our favour or against us. If, therefore, we give due effect to these

consideration-liabilities, our books will give full particulars of the mutual indebtedness of traders, as well as of the acquisition or loss of individual wealth.

It is a simple matter to set the liabilities due to us off against the liabilities due from us. This is done by passing money, cheques, or bills of exchange. It should be noticed, by the way, that indebtedness may often be discharged with rather less money if it is tendered promptly—this is the case of cash discounts—so that profits may be affected by the transactions expressly made to discharge indebtedness, as well as by the transactions at first creating indebtedness.

If we have made a profit, the balance of indebtedness in our favour enables us to incur indebtedness against us in our household economy, when the one kind of indebtedness can be set off against the other, just in the same way as was done in the business itself. Thus a trader's profits find their way into the banker's hands, cheques are drawn upon the banker to shopkeepers, and the indebtedness to these gets set off against the indebtedness by the banker.

While we saw just now that Bookkeeping consists in recording the consideration-liabilities of transactions duly made, it should also be pointed out that the trader may, and should, anticipate the result of future transactions, if he has put himself in a position to absolutely command transactions solely in his favour. This is the case of goods on hand. He has the goods, there can be no more liability against him for them, yet he is certain people will make themselves indebted to him in order to secure possession of his goods. It is right for him, therefore, to anticipate these future transactions at a fair price. He does this by making an entry in his books as though the goods were indebted to him, in the same way as he might have shown a person indebted to him who had bought them.

In the next place, it is most important to remember that in

every transaction two persons are concerned, and as it is the office of Bookkeeping to properly record and classify transactions it is necessary to show the double effect in each case. I cannot pay money to Brown, but Brown must receive money from me. I must have an account for myself to show that the money has gone from me; I must have an account for Brown, and show the money received by him. Hence the term "double entry." In actual practice my account will be divided into several accounts as Cash, Sales, Discount; but for our present purpose it is simplest to view these subdivisions as comprising one whole, "my account," as opposed to "my customer's account."

Now, it cannot be too strongly impressed that the double entries should be there in every case, either in detail or in total. A bookkeeper may well pause occasionally, unless he is quite familiar with his work, and say to himself, "Now I am "charging this item here: where am I allowing it?" or "I am "allowing this item here: where am I charging it?" It is not difficult to realise the double effect of the transaction where goods or cash pass, for if, in my dealings with Brown, he gets to have more goods, I must have less; or if I get to have more cash, he must have less: especially is this forced upon people by the customary routine of passing such items through Cash Book and Day Book. But it must be remembered that the items which seem to grow of themselves, or are the indirect result of principal transactions, have the double effect just the same. Take an illustration: I have to allow Brown £5 because the last lot of goods I sold him proved to be partially damaged. What must I do? Deduct £5 from the amount owing by Brown. That is quite right; but do I stop there? No, I cannot allow Brown £5, but I must lose it myself. I know that very well, for I argued with him for three-quarters of an hour in my endeavour to make him see that I need not allow him anything. If I deduct £5 from Brown's account I

must deduct £5 from the profit I make on selling goods. Again, Brown may be my landlord, and in course of time rent becomes due to him; I deduct the amount from his account, but this is also a loss to me, and I must deduct it from my profits.

Three-quarters of the bad Bookkeeping in small businesses is due to a want of care in this respect. A few items are treated for only one of their effects; the entry gets into the customer's account, because we are forced to agree money with him, but the effect the item has upon the firm's own business is calmly ignored. So, for the want of a little care at the time, a large amount of trouble is occasioned in picking up stray items, if ever the books have to be properly balanced. The white sheep have been safely herded in the pen, but the black ones are hidden away in every conceivable dark hole and corner. Let it be remembered, then, that as it takes two persons to make a bargain, so two persons are affected by a transaction, and accordingly two accounts should in theory be altered, whether we choose to be at the trouble or no. As a nail which it is intended shall hold, so let this fact be driven home and clenched.

Having decided that every transaction should properly affect two accounts, we have in the last place to notice that this effect is the reverse in one account to what it is in the other. Take our dealings with Brown:—If I receive, Brown pays; if Brown's goods are increased, mine are reduced; if Brown owes money, money is owing to me; that which increases Brown's gains, (by itself) reduces mine. Everybody knows this, for the buyer wishes always to lower the price, the seller to raise it. We may settle it then that if we know the effect a transaction will have upon one account, we may be sure it will have the reverse effect upon the other account. There are no exceptions to this, and it is the reason why books properly kept must balance.

We see, therefore, that all commercial wealth and indebtedness depend upon the monetary considerations of individual transactions; that there are two persons affected by every transaction, and two accounts to be altered; and that a transaction has the reverse effect upon one account to what it has upon the other.

CHAPTER II.

The several Accounts which a Business Man will keep to show his Affairs.

Accounts with Customers—Cash and Banking Accounts—Compelled to keep these—Hence "Single Entry"—Advantage of Complete System—Meaning of Capital Account—How Gain shows itself—Profit and Loss Account and its Relation to Capital Account—Subordinate Accounts to Profit and Loss Account—Property Accounts—Finally, Four Classes of Accounts the Foundation—Illustration.

A BUSINESS man will open an account with every person with whom he has dealings, excepting in some minor cases—generally when cash passes against each transaction—where he may think this unnecessary. He will also have a Cash Account, and, most probably, a Banking Account. If he is his own cashier, the Cash Account simply shows receipts and payments, and the amount of cash he should have in hand at any time. If he employs a cashier, then it is in precisely the same form, and is virtually a running account with that cashier. Cash Account and Banking Account are most readily understood, if looked at as the accounts with cashier and banker respectively, worked precisely on the same lines as an ordinary customer's account, and showing a balance due to or from cashier and banker, just in the same way as a customer's account shows a balance. His object in keeping these two accounts is also, no doubt, to assist him in entering up his customers' accounts; but this is

not our present point, for he keeps other records, that are not accounts at all, to assist him in entering the customers' accounts.

Thus much the everyday administration of his business compels him to do. He must know how much people owe him, so that he can demand payment; he must know, from his own books, how much he owes to others, so that he can check their statements demanding money, with the items which he has allowed in his books as owing. So, to see that he is fairly done by, and possibly, also, to see that he does fairly by others, he will have accounts with the persons with whom he is in the habit of dealing. Having made one entry for each transaction, viz., the entry affecting the person's account with whom he deals, he will often rest content and trust to Providence for the rest, and to time ultimately demonstrating—as, be assured, in a rough manner, it will, some day—whether, on the whole, he has grown richer, or whether, on the whole, he has grown poorer, as a result of those transactions. It is then said that his books are kept by "single entry." He can, of course, form a rough idea of the changes in his position by periodically taking stock of his affairs, though, if he will be at this trouble, he will probably be willing to carry his Bookkeeping further.

But, if he wishes to make his Bookkeeping complete, he will have an account showing his stake or interest in the business, and accounts showing the various effects his dealings have as tending to increase or diminish that stake, and to one or other of these accounts he will make parallel entries to those he has made in the personal accounts. This will show him how much he makes on the sale of his goods, and how much has to come off for different expenses; he will be able to compare the volume of his trade with that of other years; he will be in a position to satisfy the income tax assessor as to his profits, and will have a tremendous advantage, through the

books balancing, in preventing inaccuracy or fraud. In the case of fraud, a single entry could be so easily smuggled in where it would not be detected. A periodical stock-taking of affairs, as mentioned in the last paragraph, may be very misleading, as there might be withdrawals or payments in of capital, or expenditure on improving business premises and the like, which may be easily overlooked afterwards. He might think his improved position was due to profits, when it might be largely due to a sum of money having been paid by him into the business. All fear of this is avoided if the accounts are fully kept.

It is to be noticed that, in what is called "single entry," much of the foundation for double entry is usually found in Cash Book, Day Book, &c., so that while we have most of the work we have none of the advantages of double entry. The terms "double entry" and "single entry" are generally understood, but it is only with reluctance that one can use them. The latter appears hardly to deserve a name, and to be looked upon as a system. It would seem truer if they were termed respectively "Bookkeeping" and "Imperfect Book-keeping."

Suppose, therefore, that the trader does not wish to trust blindly to Providence and time, and decides to keep accounts to show the effect his business is having upon his own position, he will fix upon the accounts and give them suitable names. The first and most important one will be Capital Account. It will show the stake or interest he had in the business at the last date of balancing the books. On the commencement of a business this account usually starts with a large payment of cash, which the trader proposes to appropriate to the purposes of the business. If he joins an existing business his Capital Account will usually commence with a cash payment in the same way. Suppose a man commences business with £1,000 which he places to his Capital

Account. He spends it in buying wheat, buys machinery without paying for it, grinds wheat, sells flour, pays wages. Now let us see where his capital is. He no longer has it in a solid lump of cash, but if his business has paid its way his capital is there just the same. We will assume he has made neither profit nor loss ; let us see how his capital is there. He reckons up all the sources from which he could raise money. These he calls "assets," and finds them to be :—

Customers, owing by them for flour	...	£1,100
Machinery in use, value ...	... ...	200
Wheat in mill, ,, ...	... ...	200
Total	... ...	£1,500

Though he can raise this amount he must not think of keeping it all for himself, for there is—

Owing to maker of machinery	... ...	£200
,, farmer for wheat	... ...	300
Total	... ...	£500

These he calls "liabilities," and if he discharged them out of what he could realise from the assets he would find his capital as at the first. His capital then comes to be represented not by a single amount of cash, but by the surplus of his assets over his liabilities—that is, the money he would have if he wound up and closed his business.

If there were two or more partners owning the business, the surplus of assets might be due to them in any proportions ; the only difference would be that each partner would have a Capital Account showing his share in the surplus. Thus, in the above example, in place of the one Capital Account we might have had Cooke's Capital Account, £601 ; Taylor's Capital Account, £399 ; the rest of the accounts being unaltered.

But the business is carried on for the purpose of gain, and this gain shows itself in the assets increasing in amount faster than the liabilities. The miller buys wheat, leaving liability £1,000, and makes it into flour worth £1,050, *i.e.*, gain £50—increase of asset over liability £50. Or, instead of the asset growing, as in this case, the liability may shrink. Thus, a rent collector collects £100; his liability is therefore £100, his asset £100, but on reckoning 5 per cent. commission, his liability is reduced to £95. In either case the result is the same, namely, the increase of the surplus asset. In reality, a man does not go into business for an abstract thing called "profit," although he may say so; he goes into business to get this surplus of assets so that he can apply it to his personal comfort. Profit is only the measure of the growth of the surplus.

Gain or profit, then, is the increase of surplus assets (in practice usually during a given period, say the current year). But we have seen that surplus assets were capital, and, as profit is the increase of the surplus, therefore profit is the increase of capital. We know that, in reality, the capital will fluctuate from time to time whenever any business is conducted, but it would be inconvenient to be ascertaining the amount of capital from day to day, so the various sums which go to make up the difference are placed to appropriate accounts, which are ultimately grouped in one called Profit and Loss. The Profit and Loss Account is, then, a collection of all the items tending to an increase, or decrease, of capital, to remain there until a suitable time, say, the end of the year, when the net difference will be added to (or, in the event of a loss, deducted from) the capital. Now, as the capital at the first was the original surplus of assets, and as the net increase of the surplus has been accounted for in the Profit and Loss Account, and as the difference of Profit and Loss Account has gone to the Capital Account, then it follows that the present capital will agree with the present surplus of assets: if it does not, there is a clerical inaccuracy somewhere.

The method in practice is simple, for the capital, when settled at the end of the year, ranks amongst the liabilities, and the Profit and Loss Account just balances against the increase of surplus assets which has been accruing since the amount of capital was fixed.

To make the point clearer, we might say that the capital corresponds to the old wood of a tree, and the profit to what we call the "young wood." As the young wood represents the last year's growth and is added to the old growth of the tree, ceases to be called young wood, and gives place to another succeeding year's growth; so the profit represents the last year's growth of surplus, and is added to the old growth (capital) and gives place to a succeeding year's profit.

Most likely the trader withdraws money from his business by which he directly reduces his capital. or, we might say, his profit; but this does not alter the above conclusions.

In the case of companies the profit is not carried to the capital but remains distinct, and the capital remains as originally subscribed. This is more convenient, under the circumstances, but the partnership way, as described above, suits our purpose better in considering the theory.

After the Capital Account, the Profit and Loss Account is, therefore, the next most important, as showing how the capital has increased or diminished. All items tending to increase or diminish capital could go to Profit and Loss Account direct, but it is usual to have a number of subordinate accounts for sales, purchases, wages, discount, rent rates and taxes, travelling expenses, office expenses, or for any other class of items that arise in the business, and the totals of these are carried, at the end of the year, to Profit and Loss Account. The object of these separate accounts is that, instead of the Profit and Loss Account containing an unwieldy mass of detail, it shows, in separate sums, the total sales, total purchases, total wages, etc.

The only other class of accounts, then, will be the Property Accounts, showing the value of such assets as real property,

machinery, stock-in-trade as valued at balancing, goodwill of business, leases, patents, ships, shares in companies, and the like.

The whole essence of the plan of Bookkeeping centres round the four classes of accounts—Asset Accounts, Liability Accounts, Capital Account, Profit and Loss Account. It often seems complicated through the mass of detail, but the mental perception is often cleared by remembering that, after all, each of these numerous details only belongs to one of these four classes. A thousand book debts will ultimately be grouped in the Balance Sheet as one asset.

The two Balance Sheets given below are in the simplest possible form, and may help to confirm the above conclusions:—

BALANCE SHEET 1895.

Liabilities	£1,500	Assets	£2,500
Capital	1,000		
	£2,500		£2,500

BALANCE SHEET 1896.
(This after a year's trading.)

Liabilities		£1,500	Assets	£2,700
Capital ..	£1,000			
Add per Profit and Loss Account ..	200			
		1,200		
		£2,700		£2,700

PROFIT AND LOSS ACCOUNT 1896.

Amount carried to Capital Account ..	£200	Amount corresponding to increase in surplus assets ..	£200

CHAPTER III.

The Use of the Descriptions "Dr." and "Cr."

Meaning and use of "Dr." and "Cr."—The Ledger *the* Book of Account—Application of "Dr." and "Cr." to Impersonal Accounts—to Capital Account—to Profit and Loss Account—to Accounts subordinate to Profit and Loss Account—to Stock-in-Trade—to Property Accounts—to Artificial Liabilities and Artificial Assets—A Debit and Credit Entry for every Sum.

A DEBTOR (Latin, *debeo*, I owe) is a person who owes money; a creditor (Latin, *credo*, I trust) is one to whom money is owing. Thus much we could even have learned from the Bible: "There was a certain creditor which had "two debtors, the one owed five hundred pence, and the other "fifty. And when they had nothing to pay he frankly "forgave them both." A beginner may make the distinction clear by remembering the old "debtors'" prisons, and that in a case of insolvency it is the "creditors" who have to be summoned to decide what shall be done. We must be perfectly clear upon this point, because we familiarly speak of a man being "in debt" or having a lot of debts, when what is troubling him is that he has such a lot of creditors. "In "debt" here means in debt to other people, *i.e.*, to his creditors.

We have seen that every transaction tends to the creation of an indebtedness. The method that has been determined by ancient custom for distinguishing the indebtedness to or against

us is the use of the terms "Dr." and "Cr.," and the reserving a separate column on the left-hand side of an account for debit items, and a column on the right-hand side for credit items. The money value of every transaction must be placed in one or the other column, according as it tends to make the person a debtor or a creditor. After several transactions we may know in our minds that a certain person is a debtor to us; nevertheless, we credit him with all items that have in themselves tended to make him a creditor, as well as debit him with all items that have tended to make him a debtor. The result will then be what our mind roughly told us it would be, and we have every detail at hand for agreeing the balance with him.

The book which tells a trader his position and his relation with others is the Ledger. It is *the* book. As an old city contained the citadel, guardhouse, guildhall, cathedral, and the homes of the citizens, so the Ledger contains in its various accounts the knowledge of affairs; and as the wall, moat, and towers existed only for the protection of the city, so the subsidiary books—Journal, Day Book, Invoice Book—are only to be viewed, in the study of Bookkeeping, as a support and outwork to the Ledger. They have another use, certainly, and that is to be a museum for the preservation of minor details, but this is no part of theoretical Bookkeeping. As the huntsman fixes his eye upon the game, and only occasionally glances at the intervening ground, so the bookkeeper must fix attention upon the Ledger, and the place that items should take in it, while arranging the groundwork in the subsidiary books. All the accounts mentioned in the last chapter are therefore Ledger Accounts.

Now, the terms "Dr." and "Cr." are applied to Nominal (or Impersonal) Accounts, that is, those showing the effect of the trading upon the trader's own position, with rather less simplicity but with as much propriety as they are to the Personal

Accounts. On what ground, then, can we justify the use of the terms to Nominal Accounts? For no other reason than that they are a person's accounts after all, the person being the owner of the business. They are his accounts which, when all grouped together, will show his position in the business. Take Capital Account; practically speaking, all the other Nominal Accounts will be ultimately merged into it. It is the account of William Dunmow, who owns the Ledger and business. He has capital employed in his business, therefore the balance of the Capital Account will be Cr. :—

(1) Because, when he first began business, money paid in by him would be debited to Cash and credited to his account, just the same as money received from a customer would be debited to Cash and credited to the customer's account.

(2) Because capital corresponds to the excess of assets over liabilities, and assets are Dr.; the equilibrium is therefore maintained by Capital a credit.

(3) Because, if Mr. Dunmow realised and closed his business, he would have to be paid the amount of his capital in the same way as a trade creditor would claim to be paid, the only difference being that the trade creditor has a sort of preferential claim.

This will, perhaps, be most easily understood if it is looked at as though the owner of the business were creditor against his cashier for the money in the business; that is, as though the cashier owed his master the capital in the business. This would be actually the case if everything were realised in cash. But his Capital Account might work out Dr. This would mean that Mr. Dunmow was debtor; that his cashier required money from him to pay the liabilities of the business; that the business in itself is insolvent. If a business is insolvent it means that the liabilities (*i.e.*, credit balances) exceed the assets (debit balances); therefore, to keep the equilibrium, Mr.

Dunmow, by his Capital Account, will be a debit balance for the difference.

The argument based upon the equilibrium is given because an item is often most easily seen to be either a debit or credit when looked at in relation to the equilibrium. But the equilibrium is not the first consideration, and it would not be right to maintain it if the items balancing across were not also themselves correct. Fortunately, if the items are themselves correctly treated the equilibrium naturally results, so that if we are in doubt as to whether an amount is Dr. or Cr., we can find confirmation by considering whether the item balancing against it is Dr. or Cr., although to have each item correct in itself should be our first and main object.

It may here be remarked that the Ledger, like a phonograph, re-tells truth or falsehood just as it has been told to it. It has no mystic powers; has not the pretensions of an oracle. Therefore if the Capital Account shows a Dr. balance, it only indicates insolvency so far as the Ledger has been given the whole facts. The Capital Account might show Dr. when the trader had withdrawn large sums against larger earnings for the current year, being made but not yet ascertained, and the business in reality might not be insolvent at all. In such a case the Ledger cannot be told the whole truth until the end of the year.

It is on precisely similar lines that we justify the terms "Dr." and "Cr." to the Profit and Loss Account. A profit is credit:—

(1) Because profits swell capital, and capital is Cr.;

(2) Because profit manifests itself by assets further overtopping liabilities. Assets are Dr.; to balance against this we want more Cr.; viz., Profit Cr.;

(3) Because the owner of a business can claim payment to himself of the amount of the profit; the owner of the business is, in fact, the creditor.

A loss will, of course, have the opposite result, and appear Dr.:—

(1) Because a loss means reduction of capital, and capital is Cr.; so a loss requires to be Dr. to come against the balance of Capital Account.

(2) Because a loss manifests itself by liabilities outgrowing assets. Liabilities are Cr.; to balance against this we require more Dr.; viz., Loss Dr.

(3) Because, if money has been lost, in order to keep the capital intact, the owner of the business must pay in the amount of the loss to his cashier; in this sense he is a debtor. Or, perhaps, it would seem clearer if we imagined the owner to have no capital in the business, but private means. Then he is Dr. for the loss, because he would be obliged to pay in money to the amount of the loss, in order to make the assets sufficient for paying everyone in full.

Now, if we can justify the terms "Dr." and "Cr." to a net profit or a net loss, whichever the result of the trading may show, we can justify, on the same ground, the use of the terms to the accounts which show the different influences which have been at work in producing the profit or the loss. The influences that contribute to a profit are, of course, Cr.; those which contribute towards a loss are Dr. They are like good spirits and evil spirits contending with one another in the affairs of the trader. One set are tending to produce assets—they are the good spirits. The other set are tending to produce liabilities (or reduce assets)—they are the evil spirits.

Every trader knows which are the good influences and which the bad. The best influence in increasing assets, and, therefore, producing profits, is the amount of the *sales*. Other examples are *commissions* earned, or *discounts* allowed to the trader; the commission tending to increase assets, when he can charge men with the amount, and the discounts allowed

to the trader going towards reducing the liability. All these are *credit* therefore.

The most potent influence in increasing liabilities is the amount of *purchases*. Other items increasing liabilities or reducing assets are *wages*, *rent* payable, *discount* allowable, *carriage*, and business and office expenses generally. All these items will, therefore, have to appear *debit*.

The credit items are those which a trader naturally seeks to make as large as possible; the debit ones are those which he tries to make small. He knows he cannot have the credit items without incurring something for the debit items, but he does what he can; he buys in the cheapest market and sells in the dearest. Obviously, it would pay him best if he could get his commodities given. We may know the debit items by their unpopularity.

The stock-in-trade, at the beginning of a trader's financial year, is placed as a debit to his Profit and Loss Account. This may cause some surprise at first sight. It will be dealt with further on; meanwhile it may be explained that it can be regarded as being a part of the purchases, and, therefore, placed on the debit side of the account with them. It is like bought from the previous year's trading, instead of being bought from persons, as the purchases proper are. Or, again, it is debited because it was an asset but has been absorbed in the business, without being otherwise accounted for. The manufacture, or business, has used this stock up and sold it, just as much as the other stock which has been bought in the year. The other goods have been debited by entries in Purchases Account, based upon invoices received in the year; this stock, at the beginning, requires debiting for a similar reason.

For example, when you last balanced the accounts you included your stock in your Balance Sheet as an asset—supposé it was for the year 1895, £1,000. Now, in 1896 you look over

your yard or warehouse and make an inventory and valuation of what you find there, and the total value—£1,500—you bring into your books and Balance Sheet. But what about the £1,000 which still stands in the books as the 1895 asset? This is no longer an asset, it has been absorbed in the business and been replaced by the £1,500; indeed, a good part of the 1895 goods may be actually included as part of the stock valued at £1,500. You must account for the absorption of the 1895 stock as though it were a loss in your business: hence you must debit it to Profit and Loss Account.

In a similar way the stock at the end of the year should be credited to Profit and Loss Account, because its value should be included with the sales; it might actually have been made one of the sales if we had called in an auctioneer to force a sale; it can be looked upon as sold to the next year's trading. But, further, it is an asset not introduced into the Ledger until you are on the verge of balancing, and only then after looking round your premises and seeing what you have. As the stock at the beginning is an asset absorbed or lost in the business, so the stock at the finish is like an asset found and therefore tends to a profit.

We have still to justify the use of the terms "Dr." and "Cr." to two more classes of accounts. The first of these is the class known as Property Accounts. They are the accounts which show a trader the value of his impersonal assets, as for example, a warehouse, a ship, or shares in a company. These accounts will appear debit. Thus if you paid £5,000 for a warehouse, you would credit the amount in your Cash Account and debit Warehouse Account, exactly in a similar way to debiting a person with cash paid to him. The Property Accounts are like persons who owe us money. You say you expect your warehouse or your shares to bring you in so much when sold, just as you expect your customers to whom you have sold goods to bring you in so much some day.

When it was said that purchases went to the debit of Profit and Loss Account, it was, of course, only meant that purchases of goods for re-sale were so treated. Permanent investments stand in the first instance at the amount actually paid for them, and Profit and Loss is only affected if it is found necessary to adjust the cost price to an altered value.

The other class of accounts referred to includes those which show the amounts reserved for, as estimated benefits, or disadvantages, likely to accrue in the future. A trader will—as it is termed—"write off" some of the profit shown in his books to Reserve Account. Well, what does Reserve Account or Reserve Fund mean? It means that he has made an artificial liability in his books in order to show less profit. Perhaps he is running a good deal of risk in his business, and he foresees possible contingencies in the future, so instead of showing quite so much as a profit, which is a liability to himself, he shows a certain amount as an indefinite liability, called Reserve, which he has to look to in case the contingency happens, or if it does not happen, he can put it back to his Profit Account. The Reserve being therefore an artificial liability is correctly treated in the same way as a real liability, viz., as a credit.

The following example will show:—

Ledger Balances (without the amount written to Reserve).

	Dr.	*Cr.*
Persons owing money	£100	
Persons to whom money owing	..	£250
Property	500	
Capital	..	200
Profit	..	150
	£600	£600

Ledger Balances with Reserve written off.

	Dr.	*Cr.*
Persons owing money	£100	
Persons to whom money owing	..	250
Property	500	
Capital	..	200
Reserve	..	50
Profit..	..	100
	£600	£600

In this example it will be seen that the artificial liability has been created, and to that extent the profit has been reduced. It will be readily admitted that it is far more correct to reserve a reasonable sum for an uncertain liability, or probable depreciation in an asset, than to ignore a probable contingency simply because we do not know the amount.

Large Reserve Funds (or accounts) are often built up in companies, not to secure a particular contingency, but to increase working capital, to secure future dividends, and to insure the general stability of the concern in the eyes of the public. In such cases the account is not so much an artificial liability, but, like capital and profit, an actual liability to the shareholders.

Other examples of artificial liabilities will be seen as we proceed.

In the same way that we may have estimated or artificial liabilities, so we may have estimated or artificial assets, provided the business will derive a future benefit, although they cannot rank amongst the ordinary assets, and should be shown separately in a Balance Sheet. For instance, we may have paid an amount to insure a ship for one year, but only six months of the time has expired when we wish to balance our books. The portion of premium corresponding

to the unexpired time, in such a case, will have to be credited in the Insurance Account against the full premium, so that the Profit and Loss Account will only get charged with the insurance for the period that has expired, and the amount for the unexpired time will necessarily come out as a debit, *i.e.*, as an artificial asset. We say an artificial asset because there is no intention of at any time realising any money from it, although we could obtain a reasonable portion of it if we were willing to take the underwriter off risk. Another example of an artificial asset is the amount of formation expenses not written off by a company. In this case nothing could be realised from it, but it might be said that the company derives a benefit from the expense incurred at the formation as long as it exists as a company, and it is usual to allow some portion of the formation expenses to be carried forward, as though it were an asset, within the first five years of the company's existence. A part of the expenditure on advertising is occasionally treated for a short time as an artificial asset, to save burdening the profit of the year in which the expenditure was incurred too much, and as future years will probably benefit. Artificial assets, like real ones, are debit.

Before we leave the consideration of the terms "Dr." and "Cr." we must refer to one point more.

We saw in the first chapter that every transaction affected two accounts, and that the effect upon one account was the reverse effect from that upon the other. Our practical method of representing this double and reverse effect is the making of debit and credit entries for each transaction. But every credit implies a debit and every debit a credit, even though the transaction that caused the present position happened long ago, and we know nothing of it. For example, Jones may come and say to you: "Atkins is suing me for £300 and I have "nothing to pay with." It is required to indicate the position

in bookkeeping terms. It is perfectly clear that Atkins is Cr. for £300; but is any account Dr.? Jones (or his Capital Account or Deficiency Account) is Dr. for the £300. If Atkins is a creditor someone must be a debtor, and Jones confesses he is the one; and if we do not actually debit Jones, to debit Deficiency Account in the affairs of Jones is virtually the same thing.

A gentleman the other day exclaimed: "You can't make a "Balance Sheet, there's only one item." He was in error simply because he overlooked the above rule. If there was one item there must be another. In the case he referred to there was a sum of money, say £500, in the bank belonging to one of two partners. It was a case of self-deception, for, though he called it one item, he himself used it in two senses: (1) it was in the bank, and (2) it was due to the senior partner. The bank was Dr., the partner Cr. Supposing, for the sake of argument, we had been able to point out that there was a trade creditor for £300, no doubt he would then have admitted that there were three items. He would be compelled to admit an item for capital now that the capital no longer corresponded to one item of asset; but why not admit the Capital Account just as much if it did correspond to another item?

We should remember, then, that every amount we have to deal with must be entered once to Dr., once to Cr.; that assets and losses are Dr., liabilities and profits Cr. An intelligent application of this rule should prevent us from having much difficulty in making the foundation entries in a Ledger.

CHAPTER IV.

The Use of Subsidiary Books.

Accounts for Administrative Functions in a Business form the Basis—Purchases Account and Invoice Book—Sales Account and Day Book—Cash Book—Bill Books, Returns Books, Transfer Book—Banking and Discount Columns in Cash Book—Travellers' Cash—Journal.

THE government of a country finds there are several administrative duties, which are best performed if they are classified, and certain officials set apart for the exclusive management of each. Thus we have the Admiralty responsible for matters concerning naval defence; the War Office for military defence; the Board of Trade for commerce; the judicial benches for the administration of law; the Local Government Board for local affairs. In a somewhat similar manner, a merchant finds certain administrative functions requiring constant performance. He is always buying goods, always paying cash; always selling goods, always receiving cash, always allowing discounts; and, if he be in a large way of business, he will have assistants who take charge of these duties, or some of them; but whether he has separate officers or no, certainly he will have separate accounts in his Ledger, to show him, at any time, how much he has bought, how much he has sold, how much he has paid and received, how much discount he has allowed, and also the result of whatever else he may have done or suffered in carrying on his business.

It is the buying and selling, the paying and receiving, about which he is concerned. Those who think that the keeping of Customers' Accounts is the only thing of real importance should remember that they are only kept at all to enable a trader to carry on his own business functions. His object in keeping Customers' Accounts is only to see that he *receives cash* to the amount he ought to, and thus secure *the benefit from his sales*.

If, therefore, he begins by recording his own administrative functions, he will have the basis for ascertaining his position with customers. The Administrative Accounts are few, the Customers' Accounts are many, and it is far easier to enter in the few Administrative Accounts the various transactions that effect each, and then, at your leisure, post to the many accounts of customers.

Let us take an example, still supposing we have only one book, the Ledger.* A clerk, who is deputed to look after purchases, begins an attempt to record these. As purchases tend to the creation of liabilities, the entries in the account will be debit. He, therefore, opens an account in the Ledger called "Purchases Account," and begins to enter on the Dr. side the brief details of purchases which have been made. Thus he will commence :—

Dr. PURCHASES ACCOUNT. *Cr.*

1896				
Jan. 1	To J. Smith	..	£300	
,, ,,	,, R. Wilson	..	40	
,, 2	,, C. Jackson	..	80	
,, ,,	,, R. Jones	..	30	

*It is not intended, in any way, to trace the historical development of Bookkeeping, but merely to explain the principles as clearly as may be. No doubt, historically, the Journal comes before the Ledger, and the Invoice Book and Day Book are, probably, developments from a classified Journal, but the present purpose is best served by treating the Ledger first.

This becomes his foundation. When more at leisure, perhaps the end of the week, he posts (*i.e.*, makes corresponding entries) in other parts of the Ledger where he has accounts for various persons, the same amounts but on the credit side, thus: J. Smith, Cr. £300; R. Wilson, Cr. £40; C. Jackson, Cr. £80; R. Jones, Cr. £30. But he finds it strains his neck to post from one part of a book to another part of the same; also, that he wants the Ledger so frequently when other people want it, and his purchases are so numerous, that he resolves to keep merely a list of the dates, names, and amounts in another book. From this book, then, the individual accounts can be posted to credit without injury to his neck, and the total of the amounts posted at the end of the month to the debit of Purchases Account; this will have precisely the same effect as the other method. And he gives a name to his new book—usually "Invoice Book," because the entries are based upon invoices which have come in; indeed, in some cases the book is a Guard Book with the invoices pasted in, and the posting is made from the actual invoice as checked and endorsed. Or he may choose to call it "Purchase "Journal."

This is what is termed a subsidiary book, *i.e.*, a book simply furnishing a help in entering the Ledger. In itself, it is nothing but a list, and the essential part of Bookkeeping only comes in when the items are posted to debit and credit in the Ledger. We could, as a moment ago we supposed, make the first and foundation entries in the Purchase Account in the Ledger, only this is found in practice not quite convenient; so we may look at the Invoice Book as though it were composed of leaves torn from the Purchase Account which are, theoretically, restored when the monthly totals get posted in the Purchases Account to the debit. It is well for us occasionally to look at things in this light, for it is quite possible to be engaged in entering subsidiary books without under-

standing the theory of Bookkeeping at all. The subsidiary books seem to complicate and hide many of the essential principles of Bookkeeping, and it is for this reason that the mention of subsidiary books has been postponed until after an explanation of the Ledger and the accounts therein.

The next class of functions, the performance of which it is necessary to record, is Sales. The clerk responsible for these opens a "Sales Account" in the Ledger, and (we will assume) begins by crediting it with the amounts charged for the different lots of goods sold, and posts therefrom to the debit of customers. But this becomes tedious and difficult to work with others, so he keeps a separate book (calling it Day Book), posts the total to Sales, and individual items to customers, and we then get a second subsidiary book.

The cash transactions next require to be dealt with. A separate book is kept for these, but it is really the Ledger Account for Cash. This can be proved (1) because there should be a Ledger Account for Cash somewhere, and there is usually no account for it within the covers of the Ledger, and (2) because the balance of the Cash Book is required to make a Trial Balance complete. Occasionally the balance from the Cash Book is overlooked when first putting the figures of a Trial Balance together, with the result that a discrepancy will inevitably appear. However, in a few instances an Account for Cash does appear in the Ledger, containing simply the monthly totals of receipts and payments taken from the Cash Book, and it is therefore merely a duplicate of the Cash Book without details. Still, whether we have an abridged Account for Cash in the Ledger or no, we may say the Cash Book is to all intents and purposes a Ledger Account, but used for foundation entries and therefore classed as subsidiary.

Many people suppose that the reason why cash received is entered in the Cash Book on the left hand page, and cash paid on the right hand, is because it is natural that as money must

be received before it can be paid, so receipts should be written up before payments. It may be natural, but it is certainly artistic. It is really because cash received is Dr., as being an asset, and cash paid is Cr., as a diminution of that asset. It is not so much because it is natural that receipts should be on the left hand, but in order to be in harmony with the rest of the Bookkeeping. The Cash Account or Cash Book, whichever we choose to term it, is often best understood if we think of it as the Cashier's Account. Then we see the cashier debits himself with what he receives, and, therefore, with what he owes his employer. When he receives a debt he transfers that indebtedness from the customer's account to his own account. He credits the customer to balance the customer's account, and debits himself with what he now owes to his employer. In the same way, when he pays a creditor he transfers the credit to his own (*i.e.* Cash) Account, and debits the creditor to balance.

It should be now apparent why we post from the Cash Book to the reverse side of accounts in the Ledger, which may have struck a beginner as peculiar after the way a Journal is used. The reason is that a Journal is a true subsidiary book, the only purpose of which is to prepare entries, as far as may be, for reaching their proper destination in the Ledger; whereas the Cash Book is a part of the Ledger itself (used also as a subsidiary book), and we have seen that entries always appear on the reverse side of one Ledger Account to what they do in the other Ledger Account.

As to other subsidiary books, the list of bills receivable, which is kept to record the names of drawers, acceptors, dates, and particulars how they are disposed of, is sometimes used as a medium for posting the individual items to credit of customers, and the total to debit of Bills Receivable Account in the Ledger; the book containing the similar list of bills payable is also sometimes used in the same way—to post

items to debit of persons and total to credit of Bills Payable Account; these books, then, in addition to statistical record, may also serve as subsidiary books. Sometimes separate books are kept for returns of goods bought or sold; these books are simply the opposite of Day Book and Invoice Book. If separate books are not kept, the returns can be entered in a separate part of Day Book and Invoice Book respectively, and posted on the reverse side of the Ledger Accounts, to come against the entries appearing in the main part of those books. A Transfer Book may also be used for correcting entries which have been posted in error to the wrong customers' accounts, etc.

The Cash Book, by means of columns, is also often made to contain the Banking Account (or the basis for it), and the basis for the Discount Account. If there is only a basis of the Banking Account in the Cash Book, the completed account will appear in the Ledger; or if these columns contain not only a basis but the whole thing, they then serve as the Banking Account, and are to be regarded, like the Cash Account itself, as a Ledger Account kept separate and used, nevertheless, to contain foundation entries as if subsidiary. The basis for Discount Account appearing in the Cash Book is always posted to a Ledger Account for discount.

If the business requires a good deal of travelling to be undertaken, it will be necessary to keep a Travellers' Cash Book. This will be worked on the same principle as an ordinary Cash Book. A separate part of it will be kept for each traveller; he will be debited with the amounts of cash he has received from customers, and credited with what he has remitted to the office. There will also be a column for discounts allowed, and the cash and discount will be posted to credit of customers from these entries in the Travellers' Cash. The credits in the Travellers' Cash will balance against the debits in the general Cash Book for remittances received at

the office, and reference folios will be given from one to the other. The book will thus contain what may be considered as Ledger Accounts with the travellers.

There is one more subsidiary book to mention—the Journal. This book was originally the one used to form the groundwork of all Bookkeeping. As its name implies, it was intended to be written up daily with entries as foundations for posting to the Ledger. Whatever the transaction might be, whether purchase, sale, payment, allowance—the Journal was found large enough to receive all. But this led to a deal of additional writing. For each transaction the preparation of Dr. and Cr. entries was made in the Journal, then two distinct entries had to be made afterwards, so the preparation seemed a needless duplication. Besides, transactions seem to be far more clearly dealt with, far more easily referred to and checked, when appearing in separate books. So in course of time the Journal has been stripped of nearly all its entries. But as at first it was capable of receiving *all*, so now it is extremely useful to receive *any* entries of occasional nature which cannot be dealt with through other books, or which are too few to need a separate book, such as entries for corrections, or for opening or closing the books.

It comes about, therefore, in practice that the foundation of all entries is first made in one or other of the subsidiary books, and this because it allows the work to be done in departments, it simplifies the labour of posting, and to some extent insures the entries being made in each case to debit and credit. Care should be taken, however, that the subsidiary books are arranged so as to give the least possible duplication of entries. This is done by making them for all practical purposes the (Ledger) Accounts showing the effect of the various administrative functions performed in the business.

CHAPTER V.

Adjustment of Accounts required at the time of Closing the Ledger.

See that Assets, Liabilities, and Profit will be Correctly Stated—I. Some Assets to be Introduced—Stock-in-Trade—Rent Receivable Accrued —Insurance Paid in Advance—Advertising Carried Forward—II. Assets to be brought to True Value—Value of Permanent Assets—Fluctuation and Depreciation — Methods of Adjusting Values—Wasting Assets—Bills Subject to Rebate—Provision for Bad Debts and Future Discount—III. Some Liabilities to be Introduced—Accruing Liabilities—IV. Liabilities to be brought to True Value —Trade Discount—Transfers to Profit and Loss—Profit and Loss Divided into Two Parts and a Sub-division—Application to Non-Traders.

BEFORE ever attempting to close the Ledger at balancing time, it is necessary to look over the accounts and see, first, that all assets and liabilities have been introduced up to date, and second, that all assets and liabilities stand at their true value. It is very essential that these should be correctly stated, because otherwise the true position of the business is not known, and also, unless the assets and liabilities are correctly stated, the profit will not be correctly shown either. It is also necessary to consider separately whether the Profit and Loss Account will be fairly stated for the period under treatment, because this thought may lead us to introduce what were termed, a while ago, artificial assets and liabilities. The introduction of these items is more due, in the first instance, to our desire to show the profit fairly than to our determina-

tion to state the assets and liabilities exactly, so it is well to look at things from the two different standpoints.

In order to show the application of these rules to general practice, it will be necessary to give a few examples in detail.

First, then, as to the introduction of all assets.

It should be seen that all goods delivered to customers, up to the point of stocktaking, have been debited to them; also that any commission, or other sums earned, have been duly charged.

The stock-in-trade is an asset which is only introduced at balancing time. It must be taken at a proper value, namely the cost price, or, more correctly, the price it would now cost to buy. If the goods have fallen in price since they were bought, a proportionate reduction must be made in valuing the quantity on hand. If they have risen in value since the purchase, they may be valued at the advanced price, though this is not so necessary, and prudence will often suggest keeping them still at what they cost. If labour has been devoted to improving the goods, the cost of this labour should be added; this is the case of goods in course of manufacture. But the stock must, on no account, be valued at the selling price.* To do so would be to take credit for a profit not earned until the goods are sold; not only is it not earned, but a good deal of expense will be involved before it can be earned. The fallacy of valuing stock at the selling price is seen if we suppose the case of a man buying a single parcel of goods for £1,000, and immediately saying they are worth £1,200 (the retail price), and, therefore, that he has made £200 profit, when he has not sold anything, perhaps never will, and in any case would have to rent a shop before the £1,200 could be realised.

* NOTE.—Unless, perhaps, in rare cases, where goods made to order are about complete, and yet not charged to the persons ordering.

If there be rent receivable, in order to show the profit correctly for any given period we must credit Profit and Loss Account (through Rent Account) with the portion accrued, although not yet due. But as it is not actually due and payable we cannot debit it to a personal account; we must treat it as an artificial asset for the present, and place it to the debit of Suspense Account, or carry it to debit of the succeeding year's Rent Account; in either case, it will be regarded as an asset.

The proportion of the insurance of a ship paid in advance has already been mentioned. If there be such an item, or any other heavy insurance, the unexpired portion should be dealt with at the time of balancing by crediting Insurance Account and debiting Suspense Account or the succeeding year's Insurance Account.

If extra large sums have been expended in one year in advertising, it is sometimes decided to spread the amount over two or three years. In this case an entry will have to be made at balancing time, in a similar manner to the case of insurance, so that a reasonable portion only is charged to Profit and Loss, and a fair proportion will stand as an asset.

In a rare case some commission has been known to require similar treatment, where future years would benefit. Possibly one or two other examples might be found of items requiring the same treatment. It should be noticed that while these items are spoken of as being treated as assets at the period of balancing, they are so placed as to get charged against the profit immediately on the commencement of the succeeding period, *i.e.*, just as the whole amounts were treated when first entered in the books. It should also be noticed that while the introduction of artificial assets may be reconciled in theory, great care should be taken not to overdo it, and bolster up the business unduly, for while they may have a fair appearance of being assets if we take the business as a going concern, it

should be remembered that, in the event of the business coming to an end, some of them would be practically worthless.

Having therefore seen that all assets have been introduced, the *second* step will be to see that all assets previously in the books stand at, or are brought to, their true and present value. This will require not a little care.

The proper value for an asset is the amount of money that could be realised from it at the present time. Any increase in the value of an asset since the last balancing time means a profit; every decrease in value means a loss. We saw at the beginning that profit meant nothing else than the increase of surplus of assets, and the fluctuation in value of an asset affects Profit and Loss just as much in the case of a permanent asset as a floating one.* If you sell your warehouse, or find you will be able to sell it, at £1,000 more than you gave for it, you have made a profit just as much as if the £1,000 came from the sale of the contents of the warehouse. If the depreciation of a permanent asset did not mean a loss we should not mind our assets depreciating. So, to show correctly the summary of assets and liabilities as well as the

* Note.—When we find learned justices speaking of a profit shown by a comparison of assets and liabilities in a Balance Sheet and a profit shown by a Revenue Account as though they might be two distinct and different things, it must surely be that this principle is not always understood. The balance of Revenue Account (or Profit and Loss Account) is the balance of assets over liabilities, including capital as a liability. If an asset declines in value the amount is *a loss*, if a profit is made it must be shown in increased assets. It is true we can prepare a Revenue Account, having regard only to alteration in value of floating assets, but so we could a Balance Sheet. The difference, therefore, is not whether the profit is shown by a Revenue Account or by a Balance Sheet, but whether or no the accounts have dealt with depreciation of permanent assets.

:3+50

profit, assets should be put up or down to their realisable value.

This is an excellent rule, and it should require very strong reasons to in any way upset it. Still it does seem to require a little explanation and slight modification.

In almost all cases it will be the intention to continue the business, so you will realise the assets in the ordinary course of business. Realisable value then gets to mean the price obtainable in a going concern. Assets intended to be *realised* in the course of business may be taken at cost price, when a forced sale would not produce as much; assets being *used* in the business may sometimes be taken as worth rather more than they would be if not used in the business, this should have some weight in the case of an asset like goodwill. We may, therefore, take values as in a going concern.

But further, take the assets which are intended to be permanently retained in the business, as buildings, machinery, goodwill, ships, stocks and shares, office furniture. The value of these should in theory be adjusted every time the books are balanced, but we may see some reasons for not doing so:—1st, the exact value of most permanent assets cannot well be ascertained; 2nd, to write off every fluctuation would be to confuse and obscure the ordinary trade profit; 3rd, these assets, so long as they serve the purpose for which they were bought, are to us, in this sense, worth neither more nor less than what they cost. We may say, therefore, that, as a general rule, we can ignore the *fluctuations* of permanent assets and retain them at cost; *unless*, by keeping them much above or below their realisable value, we are likely to mislead the public. According to company law, railways' "permanent "way" should, and mining property may, be retained at cost.

But whatever reason we may see for sometimes ignoring the fluctuation of permanent assets, there can be none for ignoring depreciation due to the ordinary process of wear and

tear; unless, perhaps, custom in a particular business might be alleged, or the fact that wear and tear would be replaced out of revenue from time to time. That such assets as buildings, ships and machinery, tend to fall in value through wear and tear, is a matter of common notoriety, and can be fairly estimated. We must, therefore, take the average life of such assets, and reduce them each year by an amount proportionate to the percentage of life which is yearly expiring. For example, we may expect that a ship will be serviceable for twenty years; we should say that it depreciated 5 per cent. each year. But we might also take into consideration the fact that, when no longer serviceable, the vessel will not be quite valueless. On the other hand, we might well fix our scale for depreciation so that a higher percentage would be written off during the earlier years than the later ones; because, first, through the newness getting rubbed off, we should find, if we ascertained the price to sell, that the vessel declined in value more rapidly during the first years than afterwards; and, second, in order to keep the vessel at all serviceable, the Profit and Loss Account would be burdened with a good deal of expense in patching up during the last few years. We should write off what seems fair under all the circumstances.

Next, as to the method of writing down the value of assets. It is perfectly clear that we debit Profit and Loss Account but it is open to us either to credit the asset or to create an artificial liability called "Reserve for Depreciation of Building" (or Ship or Machinery). The reserve can be deducted from the asset when preparing a Balance Sheet. If we credit the asset itself, we have it appearing at what we assume to be its correct value; if we make an artificial liability, we show in one account what the asset cost, and in another account the amount we think its value has declined. In a good many instances, the latter way appears preferable; thus, for example, while a

building may be depreciating by age and decay, it may be appreciating by a general improvement in the price of property. What a thing has cost is a tangible fact, to the owner at least; the rest is more or less estimate.

Another class of assets needing attention at balancing time are the wasting assets, as patents, or leases for a term of years. A fixed limit is placed upon the existence of these as assets, and we must see that a sufficient sum is written off them each year, so as to cause them to be expunged from the books by the time the term has expired.

The case of bills held which are not yet due, although it mainly concerns the banking business alone, affords a good example of an asset needing to be brought to its present value. This is done by allowing for a rebate. Thus, a banker gives £90 for a bill payable in the future at £100. The £10 is the consideration for risk incurred and interest on the money laid down until the bill becomes due. In the ordinary course the £10 gets credited at once to the Discount Account, but as the bill is not yet due this would be anticipating next year's profits unless we carried forward the proportion not yet earned to the next year, and reduced our asset by an artificial liability accordingly.

The book debts, in all probability, will not stand in the books at their true value. We have to see that we make due allowance for the loss which has arisen, or will probably arise, through the failure of any of our customers to meet their financial obligations in whole or in part. The most primitive method of treating bad debts is, as soon as a debt shows decided symptoms of being bad or indifferent, to write it off, or any portion, direct to Profit and Loss Account (or Bad Debt Account, which is a part of Profit and Loss Account); that is, credit the debtor to balance, and debit Profit and Loss Account. But a more scientific way is to open an account called "Bad and Doubtful

"Debts," and, as soon as a debt becomes at all uncertain, transfer the whole amount to this account, where it remains as an asset with other amounts of a like nature. But to make the position correct, an artificial liability is created called "Reserve for Bad Debts," and made equal in amount to the whole of the Bad and Doubtful Debt Account, or equal to such proportion as is thought fit. When any of the debts become absolutely hopeless we can write the amounts off against the Reserve. Take an example:—

Dr. BAD AND DOUBTFUL DEBT ACCOUNT. *Cr.*

	£ s d		£ s d
To J. Williams	20 0 0	By Cash—J. Williams's Dividend	10 0 0
,, R. Good	30 0 0	By Reserve for Bad Debts Balance of J. Williams's Debt	10 0 0
,, C. Watson	40 0 0	By Balance..	70 0 0
	£90 0 0		£90 0 0
To Balance, viz., Good and Watson	£70 0 0		

Dr. RESERVE FOR BAD DEBTS. *Cr.*

	£ s d		£ s d
To Bad and Doubtful Debt Account— J. Williams.. ..	10 0 0	By Profit and Loss ..	62 10 0
To Balance	52 10 0		
	£62 10 0		£62 10 0
		By Balance, being 15s. per £ on £70.. ..	£52 10 0

Under the first method of treatment we must lose sight of doubtful debts, or else retain them as assets for some con-

siderable time after they have become all but worthless; but under the second method we have the amounts kept in view, are more likely to see to their recovery in time, and can better estimate the probable future loss.

Not only have we to take bad debts into consideration, but if the debts are subject to a discount we must also allow for this. We will assume that if the debtors pay promptly they will be allowed 5 per cent. Therefore, 5 per cent. on the total amount of debts standing in the books at balancing time must be calculated, and the result debited to Discount Account (*i.e.*, Profit and Loss), and credited to a Suspense Account or Estimate Account. Or the amount may be brought down as a balance in Discount Account; that is, debit the Discount Account before the balance is struck, so that the extra amount comes against profit, and credit it beneath the line striking the balance. This bringing down of the balance, if resorted to, should be supported by a Journal entry in the terms, "Old Discount Account, Dr. to New Discount Account." If we carry the amount to a Suspense Account we shall, at the beginning of the next year, reverse the entry, and bring the amount to credit of New Discount Account; so the method of bringing down the amount as a balance of Discount Account comes to precisely the same thing, just saving the posting on both sides of the Suspense Account. In either method the effect is threefold—the debit for increased discount comes against the profit; for the time being the credit is deducted from the unreal value of the debts for the purpose of a Balance Sheet; and, finally, the credit comes against the discount to be allowed in the subsequent year. This is as it should be.

It will be seen that these principles apply equally to the amounts mentioned earlier, as premium paid in advance, accrued rent, &c. We may treat all these accruing amounts, whether debit or credit, either in a Suspense Account

or the New Account, and a threefold effect needs to be produced.

To see that it is correct to provide for discount to be allowed in the future off the debts, we have only to remember that £1,000 in debts subject to a 5 per cent. discount would only bring us in £950, and we must not value them at more than they will actually produce. Even if the discount is eventually not allowed in some cases by reason of the debtor's delay in paying, still the above principle holds good, for the business of next year will suffer for want of the money, and what you save on your customer's account you will most probably pay to your banker.

But further, it is necessary to provide for the discount to be allowed in order that a proportionate amount of discount comes against each year's profits, so that each separate year may show its own net profit correctly. Suppose 1895 is our first year of business, and we sell £1,000 worth of goods all subject to 5 per cent. discount, and half of these goods have been paid for and half remain owing. The next year £2,000 worth are sold, and half of this remains owing, though the balance of the first year's sales is received. The Discount Account will work out as follows :—

Dr. DISCOUNT ACCOUNT 1895. *Cr.*

		£ s d		£ s d
1895	To Discount actually allowed on £500 per C.B.	25 0 0	By Profit and Loss Account, amount transferred	50 0 0
	[To New Account, estimate on Debts ..	25 0 0]		
		£50 0 0		£50 0 0

Dr.	DISCOUNT ACCOUNT 1896.		Cr.
	£ s d		£ s d
1896 To Discount actually allowed:— On £500 debts of 1895 .. £25 On £1,000 recd. for 1896 .. 50 Per C.B.	75 0 0	[By Old Account, estimate for 1895	25 0 0]
[To New Account, estimate on Debts ..	50 0 0]	By Profit and Loss Account, amount transferred	100 0 0
	£125 0 0		£125 0 0
		[By Old Account, estimate	£50 0 0]

Now it is seen that the Profit and Loss Account gets charged for :—

1st year, £50, against £1,000 sales.
2nd ,, £100, ,, £2,000 ,,

But if no provision for estimates were made, and each succeeding year paid part for the previous year, the amounts would come quite irregularly and the profit would be anticipated. In this case we should have had:—

1st year, £25 against £1,000 sales.
2nd ,, £75 ,, £2,000 ,,

If in a third year the sales fell to £1,000 again, we should have :—

3rd year, £75 against £1,000 sales.

We now come to the *third* step. Having, by direct or indirect means, introduced and brought to their true value all the assets, care must be taken to see that all the liabilities are introduced up to date. This is, of course, in the first place, a matter of ordinary routine, but a few special points may be referred to.

We must be careful that all indebtedness for goods delivered to us or bought, up to the very point of stocktaking, is included. If goods get into stock without the liability for them being included, the profit will be incorrect. If goods have been bought but not delivered at the time of stocktaking, the invoice price should be included as a liability, and the amount added to the stock.

All accounts against the business for stores or services rendered, prior to the day of balancing, such as accounts for stationery, truckage, carriage, repairs, and professional services, should be got in, if possible, and included in the books. If the accounts cannot be obtained, it is better to estimate a reasonable sum than to omit them altogether, unless, of course, the amount is very trifling.

All liabilities accruing, as Rent, Interest, Salaries, Wages, will have to be calculated by the day, and the accrued portions debited to Rent, Interest, Salaries, and Wages Accounts respectively, and credited to a Suspense Account, or dealt with in the new accounts for these items.

Having seen that all liabilities have been introduced, it only should remain in the *fourth* place to be seen that the liabilities previously entered stand at their correct amount; but if the clerical work has been performed accurately up to date there will be nothing further to be done at balancing time, unless there be disputed claims to reserve for or a trade discount.

If goods bought have been invoiced at a price subject to a trade discount, and the gross, instead of the net, amount has been passed through the books, there will be further need for Suspense or the New Account in order that Profit and Loss Account may get the benefit of the discount, and the liability be reduced by the same amount.

In preparing a Balance Sheet all amounts for accrued assets and liabilities should be added to the other assets and liabilities

respectively, but artificial assets and liabilities, entered in the books merely to counterbalance the unreal value of other items, should usually be deducted from the items they are intended to adjust.

Finally, then, having brought all assets and liabilities to their true and present value, and a trial balance of all the debit and credit items agreeing exactly, it is a simple matter to marshal the amounts that affect the trading to the respective sides of Profit and Loss Account. If the books are those of a firm the balance of profit or loss is divided according to the agreement, and credited, or debited, to the partner's accounts. If we are dealing with the case of a company, when the shareholders have passed a dividend a cheque will usually be drawn for the total amount of such dividend and placed to a separate banking account. The Profit and Loss Account is debited with this amount from the entry in the Cash Book. Cheques for dividends are drawn upon the separate Banking Account, and any balance of this account remaining will represent dividends unclaimed, and can be brought back into the books if necessary. The profit may be further reduced by a transfer to Reserve Account, and the remainder is carried forward to the next year. In small companies, when a dividend is declared it is best to make a Journal entry, debiting Profit and Loss Account and crediting a Dividend Account. As dividends are paid the amounts are posted from the Cash Book to the debit of the latter account, and when all are paid it will be balanced off.

Hitherto we have spoken of Profit and Loss Account as one account. Most frequently it is divided into two accounts, and the first of these subdivided. The first account will be called "Trading Account." It will contain all the items that affect the year's (or half-year's) business. In the first part is shown the stock at commencement, the purchases, cost of

manufacture (if any) on the one side, and the sales and stock at the finish on the other side. The balance is then brought down and shows the profit subject to the expense of management and distribution. All further expenses or gains in the business are next shown, and the balance is carried to the second account, to which the name "Profit and Loss Account" is exclusively appropriated.

In the case of a firm the "Profit and Loss Account" will contain the following items:—The balance brought from Trading Account, any gains or losses not directly arising in the business (as *e.g.*, the effect of fluctuations in permanent assets), the interest (if any) on Partners' Accounts, and the division of the balance to the partners.

In the case of a company the "Profit and Loss Account" will include the balance brought forward from the previous year's Profit and Loss Account, the balance of Trading Account, items for any extraordinary losses or gains, transfer fees, items appropriating part of the balance, and the remainder as a balance carried down.

So far we have only spoken of accounts as those of a trader, but it only remains to be pointed out that the above principles are easily adapted to the altered circumstances if the accounts are those of a non-trader. Income takes the place of profit, expenditure the place of loss. Instead of Profit and Loss Account we shall have Income and Expenditure Account. Rents or interest can be debited to persons through a book corresponding to Day Book, and the totals credited to Rent or Interest Account, which will ultimately go to Income Account. Expenses can go through an Expense Journal, corresponding to Purchase Journal, the analysed total of which may go to Rates Account, Repairs Account, Commission Account, &c. But if there is a large property it may be well to have a separate account for each lot, and carry the net gains from each Property's Account to

Income Account. The chief point, however, to observe is that the Dr. and Cr. principle applies in a precisely similar way to the accounts of both traders and non-traders.

Our last word on this subject then will be — get the assets and liabilities correct, and the profit will be correct too.

CHAPTER VI.

Some Points of Interest in Goods and Stock Accounts.

What is meant by a Goods Account?—Example of a Goods Account—Confirms Treatment of Stock—Two Checks upon the Turnover—I. Where Turnover can be Checked by the Quantities—Method of doing it—Advantage—II. Checking Profit as a Percentage of Sales—Stock Books.

IN elementary Bookkeeping the separate accounts for purchases and sales are frequently dispensed with, and the purchases are placed directly to one side, and the sales to the other side, of the same account. At the end of the period the stock is inserted and brought down as a balance, and any difference in the totals is carried to Trading Account, or Profit and Loss Account. The account goes by the name of the particular commodity dealt in, as "Cotton Account," or "Timber Account"; if there are several commodities, there may be an account for each; often, however, an account of this nature will be kept under the designation of "Goods "Account," and we may speak in general terms of a single account dealing with purchases, sales, and stock as a Goods Account. It will be seen that we are only appropriating a name to what was described at the end of the last chapter as the first part of the Trading Account.

While it is decidedly to be preferred, as giving more information, to show the amounts of purchases, sales, and stocks in

the Trading Account, it may be profitable for once to look at the Goods Account as one whole, and consider a few points in connection with it.

An attempt has been made in Chapter III. to show, theoretically, why the stock at the beginning should be included on the same side with the purchases, and the stock at the conclusion of the period under treatment on the same side with the sales. But the accuracy of such a treatment will, perhaps, be most clearly seen by a practical demonstration of its truth with actual figures.

Suppose we carry on the business of a flour merchant, and that we always fix our selling price at 5 per cent. above the cost price. Let us work out the result:—

Dr. GOODS ACCOUNT OF FLOUR MERCHANT FOR YEAR 1896. *Cr.*

No. of Sacks.		£ s d	No. of Sacks.		£ s d
1,000	To Stock 1 Jan. 1896 at cost.	500 0 0	20,250	By Sales ..	10,631 5 0
20,000	To Purchases .	10,000 0 0	750	By Stock 31 Dec. 1896 at cost.. ..	375 0 0
	To Balance ..	506 5 0			
21,000		£11,006 5 0	21,000		£11,006 5 0
				By Balance, being Profit.	£506 5 0

It will be at once seen that the £506 5s. is no arbitrary amount, but is equal to 6d. per sack on 20,250 sacks, the number sold. Or again:—

	21,000 sacks cost	£10,500
	750 remain unsold (at cost)	375
therefore	20,250 are sold, costing	£10,125

Calculate 5 per cent. on £10,125 and it will be found to be

£506 5s.; therefore the profit shown works out at the proper percentage on the total cost of the sacks sold. We now see that the treatment of the stocks at the beginning and end is confirmed by the result.

It will be readily admitted that the gross profit should work out as an aggregate of the increase in prices charged for goods sold, and if any proof is needed to show why we get such a result by the above method, it may be pointed out that the stock to begin with and the purchases stand both on the debit side at cost prices; that the stock at the finish (that is, the unsold portion of the other two) is reckoned also at cost, and appearing on the credit side has the effect of a deduction from the debit. On the debit side, then, we have a quantity of goods, equal to the quantity sold, at cost price; on the credit side we have the quantity sold at selling price. Theoretically, therefore, the percentage will be shown in the result. Still, we should remember that the selling price will, in most cases, be the *present* price to buy plus the percentage, so on old stock we may be getting rather more, or rather less, than the percentage, and a certain amount of discrepancy may arise in this way, which, however, does not in the least affect the principle. If a merchant does not make a regular charge but gets on each transaction what he can, then the only difference will be that the profit will come out as the average of what he has charged for himself.

But we should learn a great deal more from a consideration of the Goods Account than simply a confirmation of the correctness of the usual treatment of the stock at the beginning and stock at the end of a period.

In the above example there are two important confirmations that the profit shown is correct:—

1st. The number of sacks is exactly accounted for.

2nd. There is an exact percentage of increase in the amount of the sales.

This shows that all the goods received have been properly accounted for, and all calculations of price have been absolutely correct. It should be the object of bookkeepers to be able to show similar results as far as circumstances will permit; usually one of these modes of checking can be applied. It should be our aim to see how far such desirable results can be attained in the case of manufacturers, merchants, and retailers.

In most wholesale businesses prices are not uniform—markets fluctuate, the dealer gets what he can on each transaction, or fixes his price by that of his competitor rather than by what yields a fair profit, and the average percentage of gain shown in the profit does not afford an exact check on the correctness of the turnover. We must therefore have the quantities worked out if we would apply a reliable test. If the bulk of the commodity is bought by weight and sold by weight, we shall frequently be able to check the quantities, even though it has gone through a process of manufacture, but, of course, this will not be so if the manufacturing has increased or lessened the bulk.

Thus the miller expects the weight of wheat bought to be shown in flour and bran sold or in stock, allowing for wheat consumed by his own horses and a small percentage of deficiency due to necessary waste in manufacture. But the brewer does not expect beer and grains to weigh against malt, on account of the added water. The gas manufacturer does not expect coke and gas to weigh against the coal used, but he does know about how many cubic feet of gas should be produced by the carbonisation of a certain quantity of a particular kind of coal. The oil miller will expect the seed he buys to be accounted for in weight of oil and cake.

If it is possible, in many cases, for manufacturers to check their turnover in quantities, still more frequently can it be done by merchants. We might perhaps say, as a general rule,

that most millers and all merchants who deal in one article or several articles reckoned by weight or measure, as corn, iron, timber, wool, oil, and coal, should be able to apply this check.

It is done by keeping a separate column in the Day Book for inserting weights opposite money, and a similar column in the Invoice Book. The quantities should appear opposite the price in every case. It is best not to rely solely upon another book for showing the quantities, as quantities might be inserted there and no money charged against them in the other books. A little care is sometimes needed when weights are not uniform; as, for example, the number of pounds in a quarter of wheat, of barley, and of various kinds of seed differs considerably; so coal bought as 100 tons pit weight may be sold at net weight, that is, 120 tons. To make the result true, each quantity may be adjusted in the separate column to a uniform standard, or several columns may be kept, say, one for barley, one for wheat, one for oats, and the various kinds of grain thus balanced separately.

The advantage of such a system is that, if any irregularity has occurred, like goods being sent away without being invoiced, the deficiency in quantity would appear and lead to investigation being made. Goods being sent away without being invoiced will, most probably, be due to inadvertence; it might be due to fraud, but in either case the business suffers loss. Especially is such a check desirable in cases where goods are ordered to be sent by manufacturers direct to the merchant's customers; the risk of omitting to invoice is much greater where the goods sold do not leave your own premises. If the quantities agree, we also know that the stocks must have been taken with tolerable accuracy, and therefore, that the profit can be better relied upon as correct for the given period.

Whether or no a merchant or manufacturer is able to check

his turnover in quantities, it is well just to work out the profit as a percentage, for he should have some idea what the average profit on his sales should be, and this will afford some test. It will also enable him the better to fix his prices in the future, and to estimate how much advantage might be expected from an increased turnover.

Coming to retail businesses, we shall, of course, find it impossible to make the quantities agree. Dozens of buttons, yards of silk, numbers of hats, and weight of wool, combined with countless other things, could not very well be checked in total, unless more time were devoted than the result would be worth, but we can have a check upon the money if we analyse our sales and purchases into departments. It so happens that when the turnover becomes more difficult to check in quantities, then the percentage of profit charged is usually more regular. Supposing we keep a small rural store, and we sell three different kinds of articles. The amount we add to the cost price for profit is as follows:—

Grocery	15 %
Drapery	17½%
Boots	20 %

We should then show three Goods Accounts, and we will suppose the first to be as follows:—

Dr. GROCERY. *Cr.*

1896		£	s	d	1896		£	s	d
Jan. 1.	To Stock ..	150	0	0	Dec. 31.	By Sales ..	1,208	0	0
Dec. 31.	To Purchases ..	1,000	0	0	,, ,,	By Stock ..	100	0	0
,, ,,	To Profit ..	158	0	0					
		£1,308	0	0			£1,308	0	0

We must find by calculation what the profit on £1,208 sales should be. £115 worth of sales yields £15 profit; therefore

$$115 \quad : \quad 15 \quad :: \quad 1{,}208 \quad : \quad 157\tfrac{13}{23}$$

This so far agrees with the actual result as to be highly satisfactory. If the sales had not been all properly accounted for, or the stock had been incorrectly taken, the percentage would not have been borne out. The other departments should be worked out in the same manner.

The advantage of such a system is that, first, you see whether you are making the profit you ought to make; and, secondly, if you are not making it, you know in which department the error lies.

If the articles dealt in are of larger value, yet still very varied (as, *e.g.*, agricultural implements), Stock Books, with kind of Ledger Accounts for each class of article, showing sales opposite purchases, will be a most valuable check. These should be posted from the Invoice Book and Day Book, and can be readily checked back into them.

CHAPTER VII.

Methods of Saving Labour.

The Importance of Saving Labour—I. A System should not Include Unnecessary Repetition—Example, Passing Everything Through the Journal—The Keeping of Draft and Fair Copy Books—Draft Cash Book Unnecessary—As to Omission of Details from Day Book—As to Invoice Book—II. As to Saving by means of Distinguishing Columns—Illustration thereof in a Cash Book—Use of Columns for Banking Account—Detailed Analysis of Cash by Numerous Columns.

IT is astonishing, if we think about it, what a lengthy and laborious proceeding Bookkeeping is. What a time it takes just making a few transfer entries and ruling off the accounts affected! We often think of the patience of some authors or novelists who have produced forty or fifty volumes. True! but we never think of the patience of those unknown authors who have filled great thousand-folio Ledgers, crammed full of names, dates, and figures, every figure right and in its right place; Ledgers that are only to be useful for a few years, and then ignominiously banished to the cellars or the paper mill. Dreary work it has been, not dashed off rapidly, as the mind may sometimes drive the pen at its whim, but each item carefully picked out and put in its proper place. And if the work itself has not caused bitter disappointment, as an unsuccessful novel may, still it has afforded no invigorating stimulus for the mind to vary the mechanical monotony. The telephone and typewriter have come to the

aid of the correspondent, but no mechanical apparatus has come to the aid of the bookkeeper.

It should be remembered that the bookkeeper has not only to keep his own accounts, but to check and reconcile other people's statements with his own. He is usually one of the most capable men in the office, and therefore an hour or two of his time saved each day would be invaluable if devoted to any other department of the business.

It therefore becomes of the highest importance to consider what little assistance ingenuity may be able to suggest to minimise the labour, so far as can be prudently allowed. And although some apparent short cuts do not yield all the benefit that might be anticipated, there is a marvellous difference between the use of a good system and the use of a bad one.

There are two ways in which we shall mainly seek for means of reducing labour—the first is in the avoidance of re-writing, and the second in the use of distinguishing columns in a book.

At first thought it might appear unnecessary to mention the first of these two, being, as it might seem, quite obvious to everyone, but experience teaches otherwise. Some bookkeepers have got into a fixed habit (and perhaps no class of men are by nature so conservative), and it never occurs to them that it would be possible to act otherwise than they have done; or, if it does occur, the dread of breaking loose from the conventional rule, not only practised by themselves, but frequently, also, by their predecessors in office, causes them or their superiors to take very unkindly to the thought of a change. If the system is a good one, all goes well, but unfortunately this is not always the case; so even if their custom gives them a good deal of additional trouble, still they cling to it with a chivalrous regard and are disposed to resent any suggested innovations. Hence it not infrequently happens that a system including a good deal of unnecessary repetition may still remain unaltered.

The original idea of Bookkeeping was that foundation entries for every transaction should be made in the Journal, and this custom is occasionally found still lingering. What is the result? Supposing a sale of goods is effected, the entries required will be :—

In the Journal :

W. Green	*Dr.*	£10 0 0		
To Sales			£10 0 0	

In the Ledger :

Dr. W. GREEN. *Cr.*

To Sales £10 0 0	

Dr. SALES. *Cr.*

	By W. Green £10 0 0

Here we have four entries for the one amount. Under the more modern system two entries are required—one in the Day Book and one in Green's account. The posting of the Day Book totals need hardly be taken into account, for it includes a whole month's sales in one entry. So the result is that the entries in the Journal for such a transaction are unnecessary—sheer waste of time. Nor is the Journal any more convenient for future reference, but rather less so, than the books of a system where all the sales are kept by themselves in one book and all the purchases in another. In every transaction all that has to be done is to make the two entries, the debit and credit in the Ledger Accounts ; and we must begin by making one of these entries, *i.e.*, the one to the Nominal Account, in the Ledger first, and let it be the basis for the entry to the Personal Account. Of course, for convenience, we keep the Nominal Accounts temporarily in another book, termed subsidiary, but in theory it is the same thing. The passing of

everything through the Journal is a good illustration of how needless repetition may be caused.

The making of entries at first in draft books is a most common way of unnecessarily increasing the labour. The reason frequently given for keeping a draft Cash Book is that it can be hastily written up for the purpose of keeping the balance right with the actual cash, and that at leisure the full particulars may be more carefully written into the clean copy. But it should be remembered that a Cash Book with full particulars written in at first, when all the details are fresh in mind, would take no longer doing than a fair copy takes writing up at the end of the month, and the time devoted to the draft would be thereby saved.

Not only does it take more time in the long run, but the method of re-copying the Cash Account has two other objections to it: First, it may be made an excuse for allowing the proper Cash Book to get into arrear, and with it the other accounts; and, second, it is not so satisfactory for checking if we have not before us the entries as at first made. We are obliged to examine the fair copy because it is the book working into the Ledger, at the same time we know that the original entries could have been so easily altered in re-copying if there were any desire to do so. Whatever may be said about cleanliness being next to godliness, I prefer an original book to a clean book. Keep it as clean as you can, but, before that, let it be original.

Another reason given for having a fair copy Cash Book is that some of the payments and receipts may be analysed and all the items of a similar nature, as amounts for carriage or trade charges, put together so as to be posted to the Ledger in one amount. But if every item were posted separately the extra trouble in posting individual items to the Ledger would be fully compensated for by the time otherwise devoted to sorting out the items and putting them together when

making the fair copy Cash Book, so that we are again left with the labour spent on the draft as unnecessary and profitless.

It is usual for the Day Book to contain all the particulars which were included in the invoices sent out. Now, in most businesses it would seem that these particulars might be dispensed with in the Day Book, if the invoices are press copied.* As soon as the invoices are made out and checked, the Day Book should be entered with simply what is necessary for posting to the Ledger, that is, the date, name, town of residence, and amount. The monthly or quarterly statements afterwards rendered to customers require no more particulars. After entry in the Day Book the invoices should be passed on to be press copied. On no account should the Day Book entries be left to be made afterwards from the Press Copy Book, in case now and then an invoice might be missed by the copyist. But the Day Book might be checked afterwards with the press copies. If the particulars were wanted at any time they could be obtained very nearly as quickly from the press copies (especially if indexed) as they would have been from the Day Book, and if in rare instances any invoices had been missed in copying, sufficient particulars could always be obtained from the Order Book, railway consignments, or other sources, as the total of the invoice would be already known. If press copies are made, then there is the additional advantage that the copies show exactly how the invoices went out, and, when it is remembered that the press copying is boy's work, it will probably appear that a fair amount of time would be saved by such a system.

* NOTE.—The Day Book is often so full of details that there seems no chance of introducing distinguishing columns for analysing the sales: thus the bookkeeper loses an opportunity of saving himself some time in dissecting, which has now to be done afterwards.

As to recording purchases, the quickest way is to fold the invoices as they come in and paste them into a Guard Book, endorse with date and name on the outside, and have a column ruled at the edge of the page for the amount. This Guard Book becomes the Invoice Book from which the postings are made to the Ledger. This now reduces the recording of purchases and sales to the making of lists of dates, names and amounts.

The above may serve as examples, first of the principal parts of Bookkeeping where re-copying may often be saved, and second of the way in which a system often gets to include re-copying. How much copying may be avoided depends, in each case, how much unnecessary writing the system at present includes, and no doubt a few other examples could be found. It should be remembered that there is no advantage in multiplying copies of details, but rather a disadvantage, because they may accidentally, or otherwise, undergo change in the process. Bring the original foundation of an entry as near as possible to its ultimate resting place; thus we avoid the labour of intermediate processes and secure no less accuracy.

The greatest saving, however, can be effected by the use of distinguishing columns in the subsidiary books, more especially in the Cash Book. By a little ingenuity in this way we are often able, while entering our Cash Book, to be virtually posting our Ledger at the same time and without repeating the figures, and this for some of the items of most frequent occurrence. The following example of the Dr. side of a Cash Book will illustrate the way of saving labour. We will suppose in this case we wish to deal with cash received from customers, discounts allowed customers on paying debts, and cash sales.

Dr. CASH.

		Cash Sales			Folio	Discount			Ledger Accounts		
		£	s	d		£	s	d	£	s	d
1896 Jan. 1	To R. Roberts		..		31		10	0	9	10	0
,, ,,	,, C. S...	1	0	0							
,, 2	,, J. Stubbins		..		42	1	0	0	19	0	0
	,, C. S...	3	0	0							
,, 3	,, ,, ...	4	0	0							
,, 4	,, J. Thompson ..		..		63	2	0	0	38	0	0
,, 5	,, C. S...	2	0	0							
,, 31	,, Cash Sales, total for month	£10	0	0	9				10	0	0
						£3	10	0	£76	10	0

Here it is seen that the trouble of entering discounts is reduced to a minimum by simply placing the figures opposite the amounts of cash received from customers, instead of passing entries for discount through a separate book. If they had been passed through a separate book, then, in addition to the extra trouble of entering in that separate book, we should have found the posting from that book to the customers' accounts more trouble, for here the amounts are ready to be posted with the amounts of cash, and finding and recording the folio does once for both. The total of the column (£3 10s.) is posted, at the end of the month, to debit of Discount Account.

Then take the cash sales column: it will be noticed the details of daily takings are only written this once in the books. Instead of posting to a Ledger Account for "Cash Sales" or "Sales," about twenty-six or twenty-seven amounts in a month, by means of the distinguishing column it is only necessary to post the total (£10) at the end of the month. It was said just now that, instead of the old system where the amount of every transaction appeared four times in the books,

we should cut it down to twice—the debit and credit for the Ledger Account. In this particular case we have cut it down again; we simply enter the daily sales once, obtaining the double entry by posting the total. Practically we have reduced the labour to one-quarter of what it might have been under the most cumbrous system. It is not often, however, that so great a saving can be made as in the case of cash sales.

The most common, and one of the most advantageous uses of distinguishing columns, is their adaptation to the Banking Account.

There are three methods in which separate bank columns may be used. The following few entries worked up will illustrate best what is meant :—

			£	s	d	£	s	d
January	1.	Received of T. Smith ..	9	0	0			
,,	,,	,, R. Wilson ..	30	0	0			
,,	,,	,, C. Cook ..	2	6	0			
,,	,,	Paid Bank		..		41	6	0
,,	2.	Drew Cheque on Bank ..	9	16	0			
,,	,,	Paid C. Woods		..		9	16	0
,,	4.	Received of J. Thompson ..	133	4	2			
,,	5.	Paid Bank		..		133	4	2
,,	7.	Received of W. Jones ..	75	0	0			
,,	,,	Paid Bank		..		60	0	0
,,	8.	Received of D. Brook ..	20	0	0			
,,	,,	Paid Bank		..		25	0	0
,,	9.	Drew Cheque for Wages ..	16	0	0			
,,	,,	Paid Wages		..		18	0	0
,,	10.	,, Carriage		..		3	4	0
,,	12.	Drew Cheque for Sundry Expenses	30	0	0			
,,	,,	Paid Sundry Expenses ..		..		26	0	0

No. 1 Method of entering a Cash Book with a Bank Column.

		Bank	General			Bank	General
		£ s d	£ s d			£ s d	£ s d
Jan. 1	To T. Smith	..	9 0 0	Jan. 1	By Bank	41 6 0	41 6 0
,, ,,	,, R. Wilson	..	30 0 0	,, 2	,, C. Woods	..	9 16 0
,, ,,	,, C. Cook	..	2 6 0	,, 5	,, Bank	133 4 2	133 4 2
,, 2	,, Bank	9 16 0	9 16 0	,, 7	,, ,, ...	60 0 0	60 0 0
,, 4	,, J. Thompson ..	..	133 4 2	,, 8	,, ,, ...	25 0 0	25 0 0
,, 7	,, W. Jones	..	75 0 0	,, 9	,, Wages	..	18 0 0
,, 8	,, D. Brook	..	20 0 0	,, 10	,, Carriage	..	3 4 0
,, 9	,, Bank	16 0 0	16 0 0	,, 12	,, Sundry Expenses ..	..	26 0 0
,, 12	,, ,, ...	30 0 0	30 0 0		,, Balance	..	8 16 0
	,, Balance	203 14 2					
		£259 10 2	£325 6 2			£259 10 2	£325 6 2
	To Balance in hand ..	..	8 16 0		By Balance in Bank ..	203 14 2	

No. 2 Method.

			Received into Bank	Received into Cash				Paid out of Bank	Paid out of Cash
			£ s d	£ s d				£ s d	£ s d
Jan.	1	To T. Smith	9 0 0		Jan.	2	By C. Woods	9 16 0	
,,	,,	,, R. Wilson	30 0 0		,,	5	,, Bank	..	133 4 2
,,	,,	,, C. Cook	2 6 0		,,	8	,, ,, ...	..	5 0 0
,,	4	,, J. Thompson ..	..	133 4 2	,,	9	,, Wages	16 0 0	2 0 0
,,	5	,, Cash	133 4 2		,,	10	,, Carriage	..	3 4 0
,,	7	,, W. Jones	60 0 0	15 0 0	,,	12	,, Cash	30 0 0	
,,	8	,, D. Brook	20 0 0		,,	,,	,, Sundry Expenses ..	..	26 0 0
,,	,,	,, Cash	5 0 0				,, Balances	203 14 2	8 16 0
,,	12	,, Bank	..	30 0 0					
			£259 10 2	£178 4 2				£259 10 2	£178 4 2
		To Balances	203 14 2	8 16 0					

No. 3 METHOD.

		Bank	General			Bank	General
		£ s d	£ s d			£ s d	£ s d
Jan. 1	To T. Smith	..	9 0 0	Jan. 2	By C. Woods	9 16 0	9 16 0
,, ,,	,, R. Wilson	..	30 0 0	,, 9	,, Wages	16 0 0	18 0 0
,, ,,	,, C. Cook	41 6 0	2 6 0	,, 10	,, Carriage	..	3 4 0
,, 4	,, J. Thompson ..	..	133 4 2	,, 12	,, Sundry Expenses ..	30 0 0	26 0 0
,, 5	,, Cash	133 4 2	..				
,, 7	,, W. Jones	60 0 0	75 0 0				
,, 8	,, D. Brook	25 0 0	20 0 0				
		259 10 2				55 16 0	
,, (31)	To Receipts from Bank, per contra ..	..	55 16 0	,, (31)	By Payments to Bank, per contra ..	..	259 10 2
					,, Balances	203 14 2	8 16 0
		£259 10 2	£325 6 2			£259 10 2	£325 6 2
	To Balances	203 14 2	8 16 0				

It has been the desire to call special attention to the treatment of various irregular bank items, like those on 7th, 8th, 9th, and 12th, and the above example is only a very short one. It should therefore be remembered that in reality the number of regular items like those on 1st and 2nd would, as a rule, be in much larger proportion to the irregular ones.

Now, of these three methods it will be seen that the first is by far the most lengthy. If, for the moment, we supposed the bank column eliminated, then the general column would be complete in itself, and the only thing remaining to be done would be to post the bank items in detail to a Ledger Account, just the same as the other items in the column are posted. Thus, for example, it would be natural if money is withdrawn from the bank to debit Cash and credit Bank as is done in this system. We can see, therefore, that the idea of posting everything is at the root of the system, and the addition of a separate column is an evolution from this; hence as a system it is easily understood, and is frequently found in use. But there is no style about it; the bank balance is on the wrong side; the cross entries make extra work; it is not very readily seen what the cheques were drawn for, nor from whom the payments in were received. There is only about one thing in its favour, and that is that it readily adapts itself to irregularities, like a cheque drawn for more than the amount paid.

The second system is the one usually recommended in books on Bookkeeping, and provided that nearly all the receipts and payments exactly correspond with amounts passing through the bank, or are altogether retained in or paid out of cash, then nothing could be simpler. You either receive into cash or receive into bank; pay out of bank or pay out of cash. There are no cross entries, the figures need only appear once; moreover, the system is easily understood, and the balances in the bank and in hand come together on the correct side of the book. If you receive a debt and pay part into the bank and

hold the remainder in hand it is quite simple, as on 7th January above; if you pay part by cheque and part in cash, as on 9th January, there is no difficulty. It is very nice to see the cash receipts and cash payments all together by themselves in separate columns.

But a good deal can be said against it. It is generally found that receipts and payments cannot always pass quite regularly through the bank. For instance, you cannot pay all the money you receive into the bank on the same day you receive it, some of it comes in after bank hours. To overcome this you may make a rule of each day paying in the previous day's takings and may decide to wink at the fact that the banker is debited in the Cash Book a day in advance; but there may be an objection to this, because every day you lose one day's interest on so much of that day's takings as there was an opportunity of banking, and you have the unnecessary risk of holding a larger sum of money at night. Then you receive post-dated cheques which cannot be paid in at once, and if you would be accurate in dates you must make a rather mysterious looking cross entry like that on 5th January. The details of receipts are entered as though they went into the bank in so many amounts, whereas the bank credits the total as received over the counter. Thus in the above example it would be necessary to add up the takings on 1st January in order to account for the £41 6s. which would appear in the Bank Book. And when it is remembered that the receipts, instead of being three in one day, may be any number up to 100, it will be seen that the checking of the Banking Account becomes a more lengthy affair. To obviate this last difficulty a further column is frequently introduced, headed "Details." The details then appear in it and the amounts as paid into the bank are carried into the bank column. But, further, if more money is paid into the bank than is received that day, it is necessary to

resort to a cross entry as shown on 8th January. If cheques are drawn to cover amounts only approximately known in amount, it is again necessary to resort to a cross entry; this is often the case in providing for wages or sundry small payments. Lastly, in posting the Ledger it is necessary to work from the two columns on either side, which is not quite so easy.

The third method, while least known, is probably, for general purposes, and for a system requiring only two columns on either side of the Cash Book, the best of the three. There may be a slight objection, inasmuch as the "General" column does not show the cash balance until the totals of bank entries are introduced at the month end, but in checking the balance at any other time the two bank columns can be easily brought to account. It is true that the figures of a receipt or payment which passes through the bank having to appear twice (that is, side by side) makes the system appear a trifle more lengthy than No. 2 system—a mere trifle—though this is no doubt amply compensated for in other ways. It may be mentioned in its favour that it adapts itself, in a most simple manner and without cross entries, to *any* irregularities (see 7th, 8th, 9th, and 12th above); it shows exactly the amounts as paid into the bank, with an indication in the position they take as to where they come from; it shows exactly for what purpose the cheques were drawn, and it contains in one column all the amounts requiring to be posted to the Ledger, so in posting there is only one column to watch. One particular advantage is that the cashier can begin by entering the receipts and payments (that is, receipts and payments as regards the outer world) first in the general column and then fill in the bank figures as a separate matter. This makes his work simpler, and he is far less likely to make inadvertent errors. The balances of cash at bank and in hand come together on the same side as in No. 2 system.

In some businesses, so far as possible, everything passes through the bank, and the Cash Book becomes merely a duplicate of the banker's account, and any cash transactions that there may be are dealt with in a Petty Cash Book. This is simply having separate books in place of separate columns in the one book.

Where it is only necessary that the books should record cash transactions, as is usually the case, for instance, with a charitable institution, it is often found convenient to have a number of columns on either side of the Cash Book in order to dissect the receipts and payments at the time the entries are made, with a view to ultimately furnishing the details required for the annual summary of receipts and expenditure. If the cash is balanced monthly, the monthly totals as analysed can be posted to Ledger Accounts, or they can be summarised on paper. However, it is always more satisfactory to keep a Ledger, especially if there is anything in the nature of an accumulated fund. To have these columns is not only a saving of time (not so much, however, as might at first be supposed, for it should be remembered that if everything went into a single column, it could be very quickly dissected separately), but the Cash Book shows the dissection on the face of it, and the cashier can, at any time, run his eye up the columns and more readily light upon any item he may require to refer to. It is certainly a saving of time if we should otherwise have posted individual items separately. In deciding the number and names of the columns, we should, of course, be guided by the particulars which will be required for the annual account. In some establishments so many columns are thought desirable that the Cash Account has to be kept in two books, one book containing the receipts and analysis thereof, the other the payments and their analysis. However, judgment should be exercised in adopting a number of columns, because it is possible to adopt so many that some of them will be more

burden than help. For example, a case was noticed where a separate column was set apart, amongst others, to receive an item which occurred just once a week. Thus one monthly total was posted instead of four separate items. That was a saving of time, of course! Was it though? Unfortunately the Cash Book ran into ten or eleven big folios each month, and thus the total of this particular column had to be filled in on the top and bottom of about eight or nine folios per month on the average, and the trouble of these carryings forward quite eclipsed the advantage of not having to post three items. If there are several classes of these infrequent items, it will, perhaps, be better to group them in one column, to be posted separately from where they stand in the column, or from an analysis at the foot of the column.

In Cash Books with many columns it is best to have a total column as a basis, and it should always be the first consideration to see that every receipt or payment gets into this column correctly, and the analysis can be easily made to balance across.

Cash sales in a retail store or drapery establishment can be conveniently analysed into a dozen departments, if necessary, by columns in the Cash Book. Entry sales and purchases may be analysed by the use of several columns in the Day Book and Invoice Book, or sometimes a separate dissecting book is found more serviceable. In these cases the adoption of columns is due, in the first instance, not so much to the desire to save time, as to secure the regular keeping up of the analysis.

CHAPTER VIII.

Facing Difficulties, with Illustration of the Mode of Adjusting an Insolvent Estate.

Difficulties arising—Digging deeply into a matter—Sorting out the Items—Getting to Understand the Real Position—Mistakes often made in Correcting Errors—Example showing Progressive Adjustment of Complications in the case of an Insolvent Business being Converted by the Creditors into a Company—First stage—Second stage—Third stage— Opening Books for the Company—Applying Right Principles generally.

THE bookkeeper, like many another person, will find himself at times confronted by unusual difficulties. At the commencement, reorganisation, or close of a business, or at any other time when it is necessary to record transactions with other people, as well as adjustments within the business itself, of an unusual character, he will find entries are required which may involve him in some doubt and difficulty. He puzzles in the morning over it; thinks perhaps it will *come* to him somehow after lunch, but his afternoon wrestlings give him the impression that lunch must be intended more for the refreshment of body than of mind. Next, a bright idea occurs to him that probably he will see it better in the morning. He wakes in the morning with the feeling that there is a trouble hanging over him somehow, but, for the moment, he cannot think what it is. Then he remembers those entries at the office. But, alas, for his finger nails and the scanty fringe

that still adorns——. His morning struggles are like those of the previous afternoon, and he finds no consolation until the subtle temptation comes whispering, "Leave them, for a while "at least."

Things never *come* to people simply because they wish for them. What colossal dimensions the woolsack would have to assume, if the appointment of Lord Chancellor suddenly came to all who would wish for it! It is only through labour that anything can be achieved, or that there is any merit in the achievement. The mountain did not *come* to Mahomet, but Mahomet could come to the mountain. So must we go to our mountain and burrow into its midst.

If the bookkeeper lack knowledge, he must seek it where it may be found, but it is wonderful what a lot can be done by digging deeply into a matter. If you would find coal you must dig deeply; it is no good to lose heart just because the surface of the earth does not look much like coal. You must dig deeply, dig more deeply, and dig again. There is a great art in making the most of one's knowledge. Write down all you know about anything, then write down what you know after that, and then write down what you know after that (paradoxical as it may seem); and no one will be more surprised than you are yourself at what you do know. Rome was not built in a day; and a complicated scheme or plan cannot be imagined in an instant nor perceived in one view. Set up the posts of a shed and you will then have something to hang your boards to, and, after that, there will be something worth covering with a roof, and you can at last erect a pinnacle to signalise the triumph of patience and skill. But do not bemoan because you cannot put up the pinnacle at first, or be deterred by the confusion of the pile of material that lies before you. Sort it out! This thick piece will be for a post, put it here. These will be boards, put them there. This must be meant for a rafter, it can go on the left. These boards are no

use, throw them behind. Then see what pieces may remain for door and windows.

So in accounts, do not let the mass of detail confuse you. A solicitor once jocosely remarked that "the next best thing "to not rendering accounts at all was to make them as "voluminous as possible." Sift the items out and put them together as far as possible; even the sorting will become simpler as you go on. A hundred creditors mixed up with two hundred debtors; ten or a dozen Property Accounts partly wrong in amount; old Capital Accounts and Nominal Accounts all mixed up and for different periods; Reserve Fund; estimated liability. Sort them out! When the creditors and debtors appear in total you will see better what is left to be dealt with. Say to yourself thus: This item is an asset, do I take it over? This is a liability, have I anything to do with it? This does not concern me, I will strike it out! What have we now?

If there has been anything in the nature of a re-adjustment of the business, consider deeply what has really happened and what effect it will have; make an epitome in your own words of any agreement in writing that has been come to. Next work out the necessary adjustment, in theory at least, on paper, even though you may be very uncertain about some items; then check it over and see that each is really being treated correctly. Bookkeeping is concerned with recording the real facts and the true legal position of everybody affected. Many people think their difficulty is due to a want of knowledge of Bookkeeping when it more consists in a want of understanding of the real position. In ordinary cases Bookkeeping has done much to illustrate and teach the true position, but in the case of a radical change in a business the changed position must be understood first, and the Bookkeeping must be based on that. If the real position and facts are fully grasped, usually three-quarters of the difficulty at once vanishes.

This is illustrated in the attempts that are sometimes made to correct errors. It very frequently happens that another error is made in attempting to correct the first. Supposing our customer Brown has to be allowed £3 for short weight in our goods delivered to him; it is clear we credit Brown, but what do we debit? Amongst indifferent bookkeepers, probably, one would credit Brown and therewith rest content, on the ground that he did not know what to debit; another would, perhaps, debit Discount, on the ground of the item's analogy to a discount; possibly another would debit Purchases, on the ground that items credited to persons on goods account pass through the Invoice Book: but there should be no difficulty. The point is, What are the facts? What was the entry when the error was made (for it is assumed that we acknowledge it as an error on our part)? We have simply to undo so much of the original entry as is wrong. We debited Brown and credited Sales too much at the first; we must now debit Sales and credit Brown to reverse this. We should say he was a poor sort of tailor who unpicked the waistcoat because the trousers did not fit, yet occasionally entries in books are made which do not show much greater wisdom. The circumstances may be more complicated than the instance above, but the real facts can always be ascertained, and experimental entries can be tried on paper to see if they work off rightly.

Perhaps one of the most awkward matters which a bookkeeper may be called upon to deal with is the adjustment of accounts required on turning an insolvent estate into a limited company, the creditors taking their dividend in shares. We will here illustrate a case as an example. It is admitted that such cases are comparatively rare in occurrence; on the other hand, it is a case in which the greatest difficulty and confusion may be found, and in this way may be regarded as a kind of "*pons asinorum*." If you can do this, what may you not accomplish? It will also illustrate points incidentally that are

of general interest, and particularly illustrate a mode of proceeding with difficult work.

Example showing adjustment of accounts required on an insolvent estate being taken over by the creditors and converted into a limited company.

The facts may be assumed to be as follows :—

Castellar & Co. assigned their estate for the benefit of creditors on the 1st May 1895.

On the 1st February 1896 a resolution is adopted for the formation of a company as from 1st January 1896, the creditors taking 6s. 8d. in the £ in shares as their dividend.

But creditors who prefer it can have 6s. 8d. in cash. A few do prefer, consequently other creditors will have to raise money by taking additional shares.

The accounts of the firm, although they balance, have not been closed nor adjusted.

The bookkeeper finds his balances as at 1st January to be as follows :— *(See next page.)*

BALANCES, FIRST STAGE, *1st January 1896.*

	Dr. £	s	d	Cr. £	s	d	Value of Assets appearing in statement submitted at creditors' meeting £	s	d
Thos. Castellar, Capital A/c ..	..			1,968	7	2			
Jas. Castellar ,,	1,462	6	8						
Thos. Castellar, Current A/c..	2,006	0	0						
Jas. Castellar, Salary A/c ..	88	0	6						
Edward Hunt, 1st May 1895	..			1,000	0	0			
Williams & Co. ,, ,,	..			568	0	0			
Brooks & Jones ,, ,,	..			1,209	0	0			
R. Westlake	59	0	0	..			59	0	0
J. Wedderburn	138	0	0	..			138	0	0
Radcliffe & Co., 1st May 1895	..			970	0	0			
Smith & Brown ,, ,,	..			404	0	0			
Profit and Loss A/c ,, ,,	309	0	0						
Investments A/c ,, ,,	1,500	0	0	..			180	0	0
*Small Warehouse	400	0	0						
Cash in hand	174	0	0	..			174	0	0
Stock in Trade	1,500	0	0	..			1,500	0	0
†Beadle & Co., 1st May 1895 ..	..			105	0	0			
Tomkin & Boswell ,, ,, ..	..			1,092	0	0			
4/64ths S.S. "Cyrus".. ..	120	0	0	..			100	0	0
Creditors since 1st May 1895	..			90	0	0			
Profit ,, ,, ,,	..			50	0	0			
Small Creditors at 1st May 1895	..			300	0	0			
Liquidation Expenses ..	80	0	0						
Trustee of Estate for Liquidation Expenses	..			80	0	0			
	£7,836	7	2	£7,836	7	2	£2,151	0	0

*This warehouse formed part of Thos. Castellar's Capital at the time he took James into partnership, but by the agreement it was expressly excluded from the assets of the firm. However, the entry was never made, but the warehouse can now be claimed by the private creditors of Thos. Castellar.

†Beadle & Co.'s claim was allowed in the Statement of Affairs at £205.

We know that in reality there would be more accounts, and therefore more apparent difficulty. Even in this there may seem some confusion.

In the first place we must realise what are the real facts,

and what are the altered conditions. Since the failure the partners have no legal interest in the business; the creditors take their places. The partners' accounts are therefore no longer necessary. What the creditors do concern themselves about is the total deficiency of the estate, which represents the total amount they will have to forego from their claims.

As Capital Account *credit* is the measure of the surplus of assets over liabilities, so Capital Account *debit* represents the surplus of liabilities over assets, or, in other words, the deficiency in the estate. Hence the Capital Accounts of the partners properly adjusted and taken together will correspond to the deficiency. But the partners are jointly liable; we need not go so far as to adjust accounts between them.

The assets must be brought to their true value, and as this would mean, under ordinary circumstances, a corresponding entry to Profit and Loss Account, we may commence our work by opening a Deficiency Account and transfer the partners' accounts to it, also the undivided balance of Profit and Loss Account, and the amounts required to adjust the value of the assets and the increased liability. This will have the effect of showing the deficiency to agree with that shown at the date of the failure.

In the next stage it will be seen that we commence with the balances as appearing in the last illustration, then follow with the transfer entries as they would appear in the Ledger Accounts and, in the outer columns, the balances still remaining to be carried forward.

BALANCES, SECOND STAGE, *1st January 1896.*

	Entries as in Ledger Accounts		Balances remaining	
	£ s d	£ s d	£ s d	£ s d
Thos. Castellar, Capital A/c ..	..	1,968 7 2		
To Deficiency A/c, Transfer	1,968 7 2			
Jas. Castellar, Capital A/c ..	1,462 6 8			
By Deficiency A/c, Transfer	..	1,462 6 8		
Thos. Castellar, Current A/c ..	2,006 0 0			
By Deficiency A/c, Transfer	..	2,006 0 0		
Jas. Castellar, Salary A/c ..	88 0 6			
By Deficiency A/c, Transfer	..	88 0 6		
Edward Hunt	..	1,000 0 0	..	1,000 0 0
Williams & Co...	..	568 0 0	..	568 0 0
Brooks & Jones	..	1,209 0 0	..	1,209 0 0
R. Westlake	59 0 0	..	59 0 0	
J. Wedderburn	138 0 0	..	138 0 0	
Radcliffe & Co.	..	970 0 0	..	970 0 0
Smith & Brown	..	404 0 0	..	404 0 0
Profit & Loss A/c, 1st May 1895	309 0 0			
By Deficiency A/c, Transfer	..	309 0 0		
Investments A/c	1,500 0 0			
By Deficiency A/c, Transfer	..	1,320 0 0	180 0 0	
Small Warehouse	400 0 0			
By Deficiency A/c, Transfer	..	400 0 0		
Cash in hand	174 0 0	..	174 0 0	
Stock-in-Trade	1,500 0 0	..	1,500 0 0	
Beadle & Co.	..	105 0 0		
By Deficiency A/c, Transfer	..	100 0 0	..	205 0 0
Tomkin & Boswell	..	1,092 0 0	..	1,092 0 0
4/64ths S.S. "Cyrus"	120 0 0			
By Deficiency A/c, Transfer	..	20 0 0	100 0 0	
Creditors since 1st May 1895..	..	90 0 0	..	90 0 0
Forward	..	..	2,151 0 0	5,538 0 0

BALANCES, SECOND STAGE, *1st January 1896—(continued)*.

	Entries as in Ledger Accounts		Balances remaining	
	£ s d	£ s d	£ s d	£ s d
Forward	..	..	2,151 0 0	5,538 0 0
Profit since 1st May 1895 ..	..	50 0 0	..	50 0 0
Small Creditors at 1st May 1895	..	300 0 0	..	300 0 0
Liquidation Expenses.. ..	80 0 0	..	80 0 0	
Trustee for liquidation exp'nses	..	80 0 0	..	80 0 0
Deficiency A/c—				
By Thos. Castellar's Capital A/c	..	1,968 7 2		
To Jas. Castellar's Capital A/c	1,462 6 8			
,, Thos. Castellar's Current A/c	2,006 0 0			
,, Jas. Castellar's Salary A/c	88 0 6			
,, Profit & Loss A/c ..	309 0 0			
,, Investments A/c ..	1,320 0 0			
,, Small Warehouse ..	400 0 0			
,, Beadle & Co.	100 0 0			
,, 4/64ths S.S. "Cyrus" ..	20 0 0			
	5,705 7 2	1,968 7 2	3,737 0 0	
			£5,968 0 0	£5,968 0 0

The books now show the deficiency as at the date of the failure. The new profit will reduce the deficiency, the liquidation expenses will increase it. In the third stage, therefore, we shall write these two amounts off to the Deficiency Account, and then proceed to carry out the scheme for reconstruction. It will be necessary to debit the new company with the assets, and credit it with the liabilities (if any) which it takes over; credit it with the shares which it issues, and debit the creditors' accounts with the same; then write off the balance of creditors' accounts to the Deficiency Account. It is right to debit creditors, and credit Deficiency Account, with 13s. 4d. in the £, because the creditors have agreed to forego this, or we might say that they had agreed to contribute the deficiency amongst them.

BALANCES, THIRD STAGE, *1st January 1896.*

	Entries as in Ledger Accounts		Balances remaining	
	£ s d	£ s d	£ s d	£ s d
Edward Hunt	..	1,000 0 0		
To Castellar & Co., Lim., shares & 6s. 8d. in cash	333 6 8			
To Deficiency A/c, balance written off	666 13 4			
Williams & Co.	..	568 0 0		
To Castellar & Co., Lim., shares & 6s. 8d. in cash	189 6 8			
To Deficiency A/c, balance written off	378 13 4			
Brooks & Jones	..	1,209 0 0		
To Castellar & Co., Lim., shares	403 0 0			
To Deficiency A/c, balance written off	806 0 0			
R. Westlake	59 0 0			
By Castellar & Co., Lim., asset transferred ..	..	59 0 0		
J. Wedderburn	138 0 0			
By Castellar & Co., Lim., asset transferred ..	..	138 0 0		
Radcliffe & Co.	..	970 0 0		
To Castellar & Co., Lim., shares & 6s. 8d. in cash	323 6 8			
To Deficiency A/c, balance written off	646 13 4			
Smith & Brown	..	404 0 0		
To Castellar & Co., Lim., shares & 13s. 4d. in cash	134 13 4			
To Deficiency A/c, balance written off	269 6 8			
Investments	180 0 0			
By Castellar & Co., Lim., asset transferred ..	..	180 0 0		
Cash in hand	174 0 0			
By Castellar & Co., Lim., asset transferred ..	..	174 0 0		
Forward				

BALANCES, THIRD STAGE, *1st January 1896—(continued).*

	Entries as in Ledger Accounts		Balances remaining	
	£ s d	£ s d	£ s d	£ s d
Forward				
Stock-in-trade	1,500 0 0			
By Castellar & Co., Lim., asset transferred ..	..	1,500 0 0		
Beadle & Co.	..	205 0 0		
To Castellar & Co., Lim., shares & 6s. 8d. in cash	68 6 8			
To Deficiency A/c, balance written off	136 13 4			
Tomkin & Boswell	..	1,092 0 0		
To Castellar & Co., Lim., shares	364 0 0			
To Deficiency A/c, balance written off	728 0 0			
4/64ths S.S. "Cyrus"	100 0 0			
By Castellar & Co., Lim., asset transferred ..	..	100 0 0		
Creditors since 1st May 1895, payable in full	..	90 0 0	..	90 0 0
Profit and Loss, profit since 1st May 1895	..	50 0 0		
To Deficiency A/c, amount transferred	50 0 0			
Small Creditors	..	300 0 0		
To Deficiency A/c, 13s. 4d. in the £ written off ..	200 0 0	..	..	100 0 0
Liquidation Expenses	80 0 0			
By Deficiency A/c, balance transferred	..	80 0 0		
Trustee for Liquidation Expenses	..	80 0 0	..	80 0 0
Forward	..	..	..	270 0 0

BALANCES, THIRD STAGE, *1st January 1896—(continued).*

	Entries as in Ledger Accounts		Balances remaining	
	£ s d	£ s d	£ s d	£ s d
Forward	..	..	..	270 0 0
Deficiency Account	3,737 0 0			
By Profit and Loss, profit since 1st May 1895 ..	..	50 0 0		
To Liquidation Expenses ..	80 0 0			
By E. Hunt, 13s. 4d. in the £ written off	..	666 13 4		
,, Williams & Co., ditto ..	..	378 13 4		
,, Brooks & Jones, ditto ..	..	806 0 0		
,, Radcliffe & Co., ditto ..	..	646 13 4		
,, Smith & Brown, ditto ..	..	269 6 8		
,, Beadle & Co., ditto ..	..	136 13 4		
,, Tomkin & Boswell, ditto.	..	728 0 0		
,, Small Creditors, ditto ..	..	200 0 0		
To Castellar & Co., Lim., amount reserved for contingencies	65 0 0			
	3,882 0 0	3,882 0 0		
Forward	..	..	..	270 0 0

BALANCES, THIRD STAGE, *1st January 1896—(continued).*

	Entries as in Ledger Accounts		Balances remaining	
	£ s d	£ s d	£ s d	£ s d
Forward	..	..	..	270 0 0
Castellar & Co., Lim. (the newly-formed company)—				
To R. Westlake, asset taken over	59 0 0			
,, J. Wedderburn, ditto ..	138 0 0			
,, Investments, ditto ..	180 0 0			
,, Cash in hand, ditto ..	174 0 0			
,, Stock-in-Trade, ditto ..	1,500 0 0			
,, 4/64ths S.S. "Cyrus," ditto	100 0 0			
By E. Hunt, shares issued and oddment in cash ..	..	333 6 8		
,, Williams & Co., ditto ..	..	189 6 8		
,, Brooks & Jones, ditto ..	..	403 0 0		
,, Radcliffe & Co., ditto ..	..	323 6 8		
,, Smith & Brown, ditto ..	..	134 13 4		
,, Beadle & Co., ditto ..	..	68 6 8		
,, Tomkin & Boswell, ditto	..	364 0 0		
,, Deficiency A/c, amount allowed for contingencies	..	65 0 0		
	2,151 0 0	1,881 0 0	270 0 0	
			£270 0 0	£270 0 0

The £270 is required to pay the creditors to whom the trustee is more particularly responsible. When this amount is received from the company, the whole matter will be closed.

It will be observed that the dividend of 6s. 8d. in the £ did not absorb the whole of the assets by the amount of £65. We presume that in forming the company it was wished not to cut the thing too fine, especially as some liability might still arise and the company guarantees the dividend on any such amounts. It is treated as a liability, either (1) as representing an unascertained liability, or (2) as an artificial liability, that is, a make-weight against any possible overstating of assets. Whichever way we view it, it will go to increase the deficiency and be a credit to the new company.

Having closed the books for the old business, the next thing to be considered is how to open the books for the newly formed company. In many cases, no doubt, the closing of the old books would get neglected, but the opening of the new books could not possibly be neglected for long, or hopeless confusion would arise.

The contract for formation of the company will, of course, have to be followed in every particular, but generally speaking the following method is what will have to be adhered to in starting the new books. The company is principally concerned with taking over the assets and issuing shares against them. Accounts are therefore opened for the respective assets taken over, and the total of such amounts is carried to the credit of a "Business Purchase Account." If any liabilities are taken over by the company, accounts are opened for these and the total debited to Business Purchase Account. There will then be a balance to the credit of Business Purchase Account, which represents the net proceeds of the estate and is the fund out of which the dividend of 6s. 8d. in the £ becomes payable. This amount is undoubtedly due to the creditors in proportion

to their debts; we shall therefore apportion it to them, and, for simplicity, the greater part of the balance—viz., that found due to creditors who take shares—will be carried in one amount to the credit of an account called "Sundry Share-"holders" or "Sundry Creditor-Shareholders"; and the smaller part—viz., that due to creditors who do not take shares—will go to credit of the trustee of the estate, as the company has nothing to do with paying these. But shares have been allotted to the majority of the creditors against their dividend. When shares are allotted, the shareholders are always debited with the amounts called up thereon—here the whole amount is required. Therefore debit Sundry Shareholders and credit Capital Account with the amount of shares. But creditors and shareholders being identical, and their account being debited for shares to an equal value to the amount it is credited for dividend, it will balance, excepting for the additional shares for which cash is payable, to provide funds to meet the dividend to small or dissentient creditors. Here, we presume, E. Hunt took all the additional shares.

We are now left with the assets taken over and the capital and liabilities balancing against them.

The working will be as follows:— *(See next page.)*

Opening Balances for Castellar & Co., Lim., *1st Jan. 1896.*

	Entries as in Ledger Accounts		Balances remaining	
	£ s d	£ s d	£ s d	£ s d
Capital Account—				
By Sundry Creditor - shareholders for shares agreed to be taken, viz.:—				
E. Hunt	..	333 0 0		
,, additional shares	..	100 0 0		
Williams & Co.	..	189 0 0		
Brooks & Jones	..	403 0 0		
Radcliffe & Co.	..	323 0 0		
Smith & Brown	..	134 0 0		
Beadle & Co.	..	68 0 0		
Tomkin & Boswell ..	..	364 0 0	..	1,914 0 0
Sundry Creditor - Shareholders—				
To Capital A/c for shares agreed to be taken ..	1,914 0 0			
To Cash for oddments of dividends under 20s.	2 0 0			
By Business Purchase A/c for 6s. 8d. in the £ on creditor-shareholders' claims	..	1,816 0 0	100 0 0	
(This £100 is of course payable by E. Hunt for additional shares.)				
Business Purchase Account—				
By R. Westlake, asset taken over	..	59 0 0		
,, J. Wedderburn, ditto ..	..	138 0 0		
,, Investments, ditto ..	..	180 0 0		
,, Cash in hand, ditto ..	..	174 0 0		
,, Stock-in-Trade, ditto ..	..	1,500 0 0		
,, 4/64ths S.S. "Cyrus," do.	..	100 0 0		
To Trustee of the estate for new creditors, payable in full.. .. £90 0 0				
For Liquidation Expenses .. 80 0 0	170 0 0			
To Reserve Fund	65 0 0			
,, Balance down	1,916 0 0			
	2,151 0 0	2,151 0 0		
Forward	..	..	100 0 0	1,914 0 0

OPENING BALANCES FOR CASTELLAR & CO., LIM., *1st Jan. 1896—(continued).*

	Entries as in Ledger Accounts		Balances remaining	
	£ s d	£ s d	£ s d	£ s d
Forward	..	..	100 0 0	1,914 0 0
Business Purchase A/c—*contd.*				
By Balance, being fund available for dividend ..	..	1,916 0 0		
To Sundry Creditor-Shareholders for 6s. 8d. in the £ on their claims ..	1,816 0 0			
To Trustee of the estate for 6s. 8d. in the £ to small creditors	100 0 0			
R. Westlake—				
To Business Purchase A/c ..	59 0 0	..	59 0 0	
J. Wedderburn—				
To Business Purchase A/c ..	138 0 0	..	138 0 0	
Investments—				
To Business Purchase A/c ..	180 0 0	..	180 0 0	
Cash—				
*To Business Purchase A/c	174 0 0			
By Sundry Creditor-Shareholders for oddments of dividends under £1 ..	..	2 0 0	172 0 0	
Stock-in-Trade—				
To Business Purchase A/c ..	1,500 0 0	..	1,500 0 0	
4/64ths S.S. "Cyrus"—				
To Business Purchase A/c ..	100 0 0	..	100 0 0	
Trustee of the Estate—				
By Business Purchase A/c for new creditors payable in full .. £90 0 0				
For Liquidation Expenses ... 80 0 0	..	170 0 0		
By ditto for 6s. 8d. in the £ to small creditors	..	100 0 0	..	270 0 0
Reserve Fund—				
By Business Purchase A/c ..	..	..	..	65 0 0
			£2,249 0 0	£2,249 0 0

* NOTE.—In practice these entries would appear in the Cash Book.

It will, no doubt, appear from the above example that the matter will become much more simple than it at first appeared, if only we will deal with it boldly and adjust it by successive stages, taking what first comes to hand, and then dealing with what remains.

One thing should be understood and remembered, and that is, that it does not follow that entries are wrong simply because they are different from what some reputedly wise authority would have prepared, because first, in a sense, we may all be wise; and secondly, we need not do things exactly alike. The man who appears to be a wise authority is he who has the boldness to act upon right principles, because he can always overcome a difficulty, and if at first he is not altogether wise, he soon will be. While it is well to adhere in a reasonable manner to generally understood terms and recognised methods, it should be remembered that there is no magic about the use of some dozen or so technical forms or expressions, especially if not properly understood. As it has been found in politics and religion that formulas have frequently become dead, so in Bookkeeping the slavish adhesion to accepted formulas seems often to obscure rather than help the understanding, and prevents men from seeking for the underlying truths. It is probable that many a bookkeeper who would be deeply concerned if a Cash Book had not every folio headed "Dr. Cash, Contra Cr." could not yet explain what was really signified by that heading. Being satisfied with the formula, the thoughts are no longer exercised. No two engineers would design a bridge to be constructed exactly alike, but so long as each man's bridge would bear the weight and not be unsightly, they would both be right. So in designing the form of accounts the main thing to consider is that we are acting all through upon right principles. If we act upon right principles then our accounts will be right. No catechism could be designed to give rules for every emergency in life, but

sufficient may be given to show the principle by which people should be guided. So in Bookkeeping we cannot expect detailed rules for everything.

Now in the last example Business Purchase Account might have been called by an entirely different name without any particular harm. It might have been called "Transfer of "Business Account," or it might have been called "Fiddle-"stick" if we had much preferred, and the only difference would have been that a stranger would have had to look into the nature of the account to see what was meant by "Fiddle-"stick Account." Or the account might have been done without altogether. We might have debited the assets taken over by the company and credited sundry shareholders with the total, then credited the trustee and the Reserve Fund and debited sundry shareholders. This would have given the same result, though the above is preferable, as showing that a general arrangement had been made to convert the whole business as it stood for the benefit of creditors, and also what was the net amount realised by the estate, and that it was equal to 6s. 8d. in the £.

We should be sure we are rightly applying right principles, then we need not be afraid to act.

Do not let the work get in arrear; "Act, act in the living "present." Sort out the items, search for the facts, and apply right principles.

CHAPTER IX.

The Separate Balancing of Ledgers.

Division of the Ledger into Several Volumes—Use and Treatment of the Reconciliation Account in Producing Separate Balance—How Details to be Arranged—Crossed Accounts with Customers—Advantages of Separate Balancing—Need of it for, and Mode of Entering Private Ledger—General Conclusions Favourable to Separate Balancing.

HITHERTO the Ledger has been spoken of as one book, and in theory it is most assuredly one book, however many volumes may be required to contain its information. The whole of it simply comprises the particulars of the affairs of one business, and the analysis of those particulars forms one Balance Sheet. But on account of bulk, or for other reasons, it is frequently found convenient to apportion the matter it contains to several volumes.

The point of separation is usually fixed with some regard for (1) the nature of the business to be recorded, (2) its publicity or privacy, (3) the geographical locality, or (4) the initial letters of the customers' names with whom it is transacted. Thus, we may have Bought Ledger and Sold Ledger, General Ledger and Private Ledger, North Ledger and South Ledger, A to M Ledger and N to Z Ledger.

Where there are several Ledgers it may be our desire to enter each upon such a principle that it will contain the figures for a trial balance in itself, without affecting the unity of the whole set as one book. It shall be our endeavour to see

if we can accomplish this upon sound and scientific principles, and if we can do so, we shall come more easily to the consideration of the advantages we seek to obtain by such a system.

Let us suppose, then, that we have three Ledgers :—

General Ledger	kept by the cashier.	
Bought Ledger	,,	manager.
Sold Ledger	,,	invoicing clerk.

It is most convenient to take Bought Ledger and Sold Ledger, for we can speak of the one as containing debit accounts and the other credit accounts. The entries will be made precisely as in simple Bookkeeping, with this addition, that the General Ledger will have a Reconciliation Account (or Adjustment Account) with each of the other Ledgers, and each of these will have a Reconciliation Account with the General Ledger. The cashier will open an account called "Sold Ledger (Reconciliation) Account" and debit it with the total of all amounts which he knows have gone as debits to the customers' accounts in the Sold Ledger, and credit the account with the total of all the items which he knows have gone as credits to the Sold Ledger. Instead of debiting the customer himself, he debits the Ledger where he knows the invoice clerk will have debited the amount. He debits and credits in total just as the invoice clerk debits and credits in detail. The balance of this Reconciliation Account will therefore be the same as the difference between the total of the debit balances and the total of the credit balances which appear in detail in the Sold Ledger, and it will balance with his own Ledger just the same as if he had three or four hundred debtor balances and thirty or forty creditor balances as shown in the Sold Ledger. As there is always more value of debit items in a Sold Ledger than credit items, the balance of the Reconciliation Account will necessarily fall *debit*.

The invoice clerk will open a Reconciliation Account, called "General Ledger (Reconciliation) Account," and will *credit* it

with the total of the amounts he has debited to customers and *debit* it with the total of amounts he has credited in customers' accounts. This account will, therefore, make his Ledger balance by itself. As there is more value of debit balances in a Sold Ledger than credit balances, so the Reconciliation Account, which balances against them, will fall *credit*. The two Reconciliation Accounts will have balances respectively debit and credit, and as they agree in amount, they can be regarded as cancelling each other, and the remaining balances are as if one Ledger only had been kept.

The Bought Ledger will be treated in a similar manner, only the Reconciliation Account balance will fall credit in the General Ledger (representing creditors) and debit in the Bought Ledger.

The General Ledger must balance by itself, because the cashier has, in gross, the items posted by the manager and invoice clerk, and the remaining items of the business he has posted himself. More than two subordinate Ledgers could be treated on the same principle.

The theory of the working is, perhaps, most clearly seen if we regard the three officers as borrowing and lending entries between each other. The cashier seems to entrust the invoice clerk with certain assets (or items that go to make assets); he accordingly debits the invoice clerk (that is, debits Sold Ledger Account) with the assets committed to his charge. The invoice clerk receives into his care the assets from the cashier; he accordingly credits the cashier (that is, General Ledger Account) for the kindness. The cashier is relieved of liabilities by the manager; the cashier credits the manager (that is, Bought Ledger Account) for the obligation. The manager takes over the liabilities and debits the cashier (that is, General Ledger Account) in consideration.

The case occurs to mind of a gas company which, as soon as the quarter's gas rentals are calculated, puts the figures

into the hands of its collector for collection, and makes an entry in its books actually debiting the poor man with the total quarter's rental, as though he owed it himself. From time to time, as he collects money and pays it in, he is credited with the amounts, and ultimately he is credited with the discounts allowed and *bonâ fide* arrears, thus making his account balance. Now supposing, for the sake of argument, we regard the "Sold Ledger Account" in the General Ledger as the Personal Account of the invoice clerk, then we shall see that he receives similar treatment at the hands of the cashier to what the gas collector receives at the hands of his company. This is worth bearing in mind when we come to the consideration of the advantages of separate balancing.

Examples of Reconciliation Accounts.

In General Ledger :—

Dr. SOLD LEDGER (RECONCILIATION) ACCOUNT. *Cr.*

	£	s	d		£	s	d
To Sundries—Sales per Day Book	2,000	0	0	By Cash	1,100	0	0
				„ Discounts	35	0	0
				„ Balance	865	0	0
	£2,000	0	0		£2,000	0	0
To Balance	£865	0	0				

In Sold Ledger :—

Dr. GENERAL LEDGER (RECONCILIATION) ACCOUNT. *Cr.*

	£	s	d		£	s	d
To Cash	1,100	0	0	By Sundries, total per Day Book ..	2,000	0	0
„ Discounts	35	0	0				
„ Balance	365	0	0				
	£2,000	0	0		£2,000	0	0
				By Balance	£865	0	0

Yes, it all looks very nice, but how is it to be done? This is certainly a rather grave question to answer. For the moment we may assume that the Day Book is posted exclusively into the Sold Ledger and the Invoice Book into the Bought Ledger, and if we had North and South Ledgers we should probably have North and South Day Books to correspond, or separate columns for North and South in one Day Book. The treatment of items for sales and purchases is therefore quite simple. But as one man must be responsible for the whole of the cash transactions, some of the Cash Book entries must be posted into each of the three Ledgers, and here the difficulty begins. However, if we distinguish in the Cash Book the Ledger into which the items have been posted by placing the letters G., B., or S.—for General, Bought, and Sold Ledgers respectively—opposite the reference folio, it would not be difficult to analyse on paper the cash received and the cash paid, and also the discounts that correspond between the three Ledgers. The result of the analysis could then be shown underneath the totals of receipts and payments, and the cashier could credit the Sold Ledger Account with the total of receipts to be posted there, and debit the Bought Ledger Account with the payments to be posted into it, and also treat discounts similarly. But there might be a few receipts to post into the Bought Ledger and a few payments to the Sold Ledger; these would also be shown in the analysis, and would be posted on the reverse side of the Reconciliation Accounts to the last items. The analysis would be the more easily got at with these particular Ledgers in use, as nearly all the money received would be for postings to the Sold Ledger, and nearly all the money paid for postings to the Bought Ledger.

Instead of analysing afterwards, the use of separate columns in the Cash Book has been suggested, and, provided the business ran regularly, would probably be found convenient.

Thus, if we had the three Ledgers as above, there would be a column for receipts to be posted to Sold Ledger, a column for payments to be posted to Bought Ledger, and, perhaps, a column on either side for General Ledger. This appears very simple; however, it should be remembered that there would be sure to be entries occasionally of receipts to be posted to Bought Ledger, and payments to be posted to Sold Ledger, which would arise through packages previously paid for being returned, accidental over-payments, special allowances, buying from and selling to the same person, and similar causes. These items could be included in the column with the few items for General Ledger, and that column only dissected afterwards. The discount would be less open to irregularities in this respect. It should also be noticed that if the Cash Book included a bank column, of the systems described in Chapter VII., it would be impossible to use No. 2 if we had separate columns for different Ledgers. It would be necessary to use either No. 1 or No. 3 systems.

But, further, supposing we had North, South, East and West Ledgers, and we relied upon distinguishing columns for these, we should require, on one side of the Cash Book, four columns for cash and four for discount. Many people would say it would be better to call your books over and rely on balancing all the Ledgers in one trial balance, than to be condemned all the year round to such a burdensome Cash Book. In many cases, therefore, it would be far easier not to have distinguishing columns in the Cash Book for the different Ledgers, but to rely on dissecting one column for receipts, and one for payments, at the end of each month, for, really, this could be very quickly done. Perhaps the case of items working into Bought, Sold, and General Ledgers is the only one in which distinguishing columns in the Cash Book would be of any practical utility for the present purpose.

But, again, we assumed just now that the Day Book worked

exclusively into the Sold Ledger, and the Invoice Book into the Bought Ledger—that all sales are for Sold Ledger, and all purchases for Bought Ledger. Unfortunately, however, this is by no means the invariable rule. In many businesses, especially the smaller ones, a good number of the transactions are with persons with whom accounts are crossed, that is, where goods are sold to, and bought from, the same person. The one transaction often leads to the other; thus the manufacturer exchanges goods with the merchant, the corn dealer usually sells seed-cake to the farmer, from whom he buys wheat, and so on. The purchase on the one side of the account may be trifling indeed against the sales on the other, but, all the same, it is enough to upset the uniformity.

Here, again, the difficulty is by no means insurmountable. Supposing we decide to keep these mixed accounts of customers only in one of the Ledgers—say the Bought Ledger—and post up our Personal Accounts in the first place without any regard to reconciliation, then we shall find at the end of a month that the Day Book has been posted into both Sold and Bought Ledgers. Assuming the total sales for a month amount to £1,000, and by dissecting on paper we find £900 has been posted to Sold Ledger and £100 to Bought Ledger, all that the cashier has to do is to debit his two Reconciliation Accounts with these amounts respectively, and the manager credits his General Ledger Account with £100, and the invoice clerk credits his General Ledger Account with £900. If it is preferred, separate columns may be used in the Day Book for distinguishing items to be posted to the respective Ledgers, and the analysis would be done as we went along. The objection mentioned against the extra columns in the Cash Book does not apply here, as there is no complication with bank and discount.

But supposing these mixed accounts of customers were allowed to creep into both Ledgers, then the only difference

would be that the Invoice Book would have to be analysed as well as the Day Book, and the Reconciliation Accounts treated accordingly.

Or, again, the following method would be possible. The whole of the sales might be posted to Personal Accounts in the Sold Ledger and the whole of the purchases to accounts in the Bought Ledger, with the result that where there had been mutual dealings there would be two accounts for the same person, one in debit in one Ledger, one in credit in the other. On the occasion of a settlement, or at other times, the smaller of these accounts could be set off against the other. The cashier would pass an entry crediting Sold Ledger and debiting Bought Ledger for the amount. The invoice clerk would credit the customer and debit General Ledger, and the manager would debit the Personal Account and credit General Ledger.

A little care would also be needed to see that returned goods, interest on current account, etc., were treated in a similar manner to the principal items.

But in order to induce people to undertake the extra trouble (or what at first appears to be extra trouble) it is necessary to be able to show some considerable advantage to be derived from the system. The following arguments may be urged in its favour :—

1st.—Each Ledger is complete in itself. Each officer can see whether his own book balances without having to wait for the others to bring up their work, and he has not to depend on their accuracy but only upon his own. In the above example the cashier could prepare an approximate Balance Sheet of the affairs of the business at the shortest notice, and long before the details of debtors and creditors could be taken out.

2nd.—We secure the localisation of errors and consequent avoidance of much of the difficulty of balancing at the end of

a period. If we can tell in which Ledger the discrepancy lies, then we have only to concentrate our efforts upon that Ledger.

3rd.—It may be claimed for the system that it helps to prevent, or lead to the detection of fraud on the part of one of the bookkeepers. It is a well-known fact that fraud is largely prevented if the books are not allowed to be exclusively in the hands of one clerk, that is to say, the one who keeps the cash should not also keep the Personal Accounts. The cashier should not be placed in such a position that he could alter the Personal Accounts to make them fit with a Cash Book from which amounts had been omitted, or in which they had been wrongly stated. Although this apportionment of duties can be arranged for without separate balancing, still with separate balancing we have a clearer demarkation of the point at which each clerk's duties begin and end, and as every item comes twice—that is, once in gross with others and once in detail—through the hands of each bookkeeper, it is far more likely that the one clerk will be a check upon the other. Supposing, with the three bookkeepers engaged as above, the invoice clerk abstracted a remittance for £10 and still credited the customer's account with the amount, although it never passed through the Cash Book. We know that in any complete system of Book-keeping this would throw the balances £10 wrong, but in separate balancing the discrepancy would be at once brought home to the invoice clerk's Ledger. The knowledge that this would be so would probably be a strong inducement to such a person to avoid an act of this nature. If the invoice clerk were guilty in this manner, as each Ledger is locked up in a separate balance he would be compelled to show the total debts to agree with the Reconciliation Account in the General Ledger. He would not have the same opportunity of increasing the amount of debit in the books by altering

a Nominal Account as he might have done without separate balancing.

Although it has been necessary to explain this third advantage at some length, it is not to be thereby understood as being of greater importance than the other two. Happily, fraud of this nature is not very frequently met with.

But whatever may be said for, or against, separate balancing in general, there is one case in which its adoption as regards one of the Ledgers appears absolutely essential, and that is where a (strictly) Private Ledger is kept. If the Private Ledger is kept by the principal, or anyone other than the bookkeeper, it is necessary that the bookkeeper should always know, without prying into the sacred volume, what is the correct amount to balance with his Ledgers, and that the principal should have by him the amount that will make the balances of his Private Ledger complete. If a Reconciliation Account is not kept, then the bookkeeper, before he can balance, must first obtain figures from the principal. Supposing he does not then agree, he will be sent back to check over his own numerous balances. Probably he will find that it is his mistake, or possibly he will come to the same result as before. At the same time the principal, because he is the principal and because only a few entries have passed through his book, will not be easily persuaded that there might be a chance of the mistake lying with him; but this is by no means impossible. While, therefore, a Reconciliation Account is essential if a Private Ledger is kept, at the same time nothing could be more simple than the manner of its treatment. In the General Ledger all things that are debits to profit are debited to Private Ledger (Reconciliation) Account, and all things that are credits to profit are credited to Private Ledger Account. Debits to partners are also debited to Private Ledger Account. Entries made in the Private Ledger the reverse way about will bring the items into form for showing

the profit and capital. The stock should not be i
into the General Ledger at all, for if the old stock an
stock appear in the General Ledger it is too apparent
Ledger what the profit will have been. The followin
entries will show the method :—

OFFICE JOURNAL.

	£ s d
Private Ledger Account .. .. *Dr.*	34,000 0 0
To Sundries—	
To Purchases	..
,, Wages	..
,, Office Expenses	..
,, Partners' Drawings	..
Sales .. .. *Dr.*	30,000 0 0
To Private Ledger Account	..

PRIVATE JOURNAL.

	£ s d
Sundries .. .. *Dr.*	
To General Ledger Account	..
Purchases	20,000 0 0
Wages	10,000 0 0
Office Expenses	1,000 0 0
Partners' Drawings	3,000 0 0
General Ledger Account .. .. *Dr.*	30,000 0 0
To Sales	..
Stock-in-Trade .. .. .. *Dr.*	5,000 0 0
To Trading Account	..

When entries similar to the above have been
bookkeeper finds that his Ledger has been cleared
private to the partners, and the keeper of the Priv
erything to hand for his Trading Account, and

to close in the usual way. It must not be supposed that the balance of the Reconciliation Account, which stands in the General Ledger, gives the office staff any clue in itself to what is contained in the Private Ledger. If the accounts for permanent assets and loans are kept in the Private Ledger, then the General Ledger only contains the balances of trade creditors, trade debtors and Private Ledger Account, and the balance of the last merely corresponds to the excess of the debtors over the creditors, or the creditors over the debtors, and in no way corresponds to the wealth or poverty of the owner of the business. Thus we might have :—

Debtors	£9,000	
Creditors	...	£10,000
Private Ledger Account ...	1,000	
	£10,000	£10,000

This does not show anything wrong with the business, it only shows that the Private Ledger is Dr. to the General Ledger; that is, that the Private Ledger must provide £1,000 to clear the liabilities in the other one, which, no doubt, with the stock and permanent assets it is amply able to do.

As the entries for a Private Ledger Reconciliation Account come only at closing time once or twice a year, there is no reason why separate balancing should not always be adopted as far as the Private Ledger is concerned.

The one objection to separate balancing is that it involves a certain amount of extra care and trouble. However, when the work has been systematically arranged, the extra trouble is not so very considerable, and is probably compensated for by an advantage not previously mentioned, viz., that each person in charge of a Ledger is likely to be more accurate in performing the routine of his work when he feels himself

solely responsible for being able to make his work balance at a given period. If, therefore, we may say that the extra trouble is counterbalanced by the inducement to extra care in performing the ordinary routine, then we are left with the more theoretical advantages to make a preponderance of argument in favour of separate balancing.

Still, if people are not grounded in the elementary principles of complete Bookkeeping, and, further, if they are not prepared to patiently devote the extra attention needed to balance Ledgers separately, it is better they should not make the attempt, else they may find they have only made confusion worse confounded.